



INSTITUTE FOR DEFENSE ANALYSES

## **The Effects of Reserve Component Mobilizations on Civilian Employers**

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June 2008

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## **PREFACE**

This document reports the work performed by the Institute for Defense Analyses (IDA) for the Office of the Assistant Secretary of Defense (Reserve Affairs) in partial fulfillment of the task entitled “Analysis of Costs to Employers Due to RC Mobilizations.” The authors wish to thank the reviewers, Dr. David Graham and Mr. Michael Fitzsimmons of IDA.

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## SUMMARY

The Office of the Secretary of Defense commissioned the Employers Economic Impact Survey (EEIS) to determine what costs are imposed on civilian employers when their employees are called up for military reserve service. The survey was administered to employers identified by reservists; it had a raw response rate of 65 percent with 999 employers responding. (The term “reservist” is used here, and throughout the study, to refer to members of both the National Guard and Reserve.) Our findings are based on the responses of 478 employers who completed the full survey and reported that they employed an activated reservist. Employers were asked about several different kinds of workplace adjustments: retraining existing personnel, paying overtime to existing employees, search and hiring costs for replacements, training costs for replacements, and wage costs reflecting the difference in pay between the absent reservist and the replacement. We report costs separately for four types of employers: small for-profit businesses with fewer than 100 employees, large for-profit businesses, private non-profits, and state and local government agencies.

In each category of employer, the majority of respondents reported no costs from reservist activation. A small number—less than 10 percent—actually benefited from activation by paying lower wages to replacements. Between 20 percent and 35 percent of employers in each category reported net costs of workplace adjustment. For those reporting net costs, the median cost varied between \$2,320 (for non-profit establishments) and \$1,880 (government agencies), with small businesses at \$2,001 and large businesses at \$1,920. In every category, 95 percent of employers had workplace costs of less than \$5,000. These costs are the total workplace adjustment costs per reservist over the duration of the reservist’s activation, on average about 11 months. Thus, most employers had workplace adjustment costs of no more than a few hundred dollars per month during their reservists’ absence. However, costs for the other 5 percent of employers were much greater in some cases. In particular, some small businesses had costs of over \$30,000, and some government agencies’ workplace costs approached \$40,000. These agencies were all first responders.

The survey also asked employers if they had lost business. While only a very small percentage of large firms reported any loss of business, around 20 percent of small businesses did so. The losses claimed varied greatly.

In addition, the survey addressed the costs of benefits paid to absent reservists. The law requires that employees continue to accrue leave during their period of active service, but only if their employer provides leave accrual for employees who are “on furlough or leave of absence.” We find that less than 20 percent of for-profit businesses provide leave accrual during activation. Employers are required to provide pension accruals for their absent reservists if the reservists make their required contributions. We were unable to quantify these costs using EEIS data; however, national data suggest that pension costs associated with reservist mobilization are not likely to be severe.

The EEIS also asked employers about their experience with reservist employees. Employers overwhelmingly rate reservists as the equal of other employees, with over 40 percent rating reservists as preferable to others. The survey found that over 40 percent of employers provided some form of voluntary support to activated reservists and their families. These expenditures included continued pay, continued health coverage for the family and various forms of in-kind support. These included care packages, phone cards, laptop computers, home repair and even making payments on car loans and mortgages.

We cannot aggregate the different elements of employer costs into a total cost for any employer or group of employers due to limitations in the design and implementation of the survey. Nonetheless, the magnitudes of reported costs, and the finding that only a minority of firms in any category experience costs, offer some guidance in considering whether employer costs should be targeted by public policy remedies.

In recent years, several bills have been introduced in Congress that would have compensated employers for their costs of reservist activations. However, no data were available on how great employers’ costs were and how many employers experienced them. The survey of employer costs provides the first systematic data on the nature and extent of the costs. Policy proposals can now be evaluated with a more complete picture of the problem they were intended to address. We consider the options of tax credits, loans, or grants to affected businesses. Our data show that employers’ costs are unevenly distributed. Therefore, an across-the-board tax credit would reward many employers with no costs and fail to fully compensate highly affected employers. Limited loan programs are already in place to help some affected small businesses. However, loans do not compensate employers for their costs; they merely defer those costs. If policy-makers

decide to pursue the goal of compensation, we conclude that the best policy would be a limited and targeted system for awarding grants. The program would require affected employers to fully document their costs to ensure that only employers with significant costs would be compensated. This requirement would also minimize the cost to the taxpayer.

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## I. INTRODUCTION

Prior to 1990, military reserve units had rarely been deployed other than as part of a total mobilization. Some reserve units served in Korea and in Vietnam; however, in both cases only a small percentage of reservists were called to active service. (The term “reservist” is used here, and throughout the study, to refer to members of both the National Guard and Reserve.) Reservists served on an individual basis in other operations, but reserve units as a whole were not mobilized. In fact, reservists were more likely to be mobilized in response to natural disasters or civil unrest than to be used to supplement active forces. Reservists could reasonably believe that they had very little chance of being called to active duty.

Today’s reservists can no longer have that expectation. The Gulf War of 1990 marked the beginning of a period in which U.S. military forces have been engaged overseas with few respites. These deployments differ from previous operations in one important respect. Although the U.S. was not engaged in total mobilization, the military services made regular and sustained use of their reserve components. The composition of forces in all four services now requires that virtually any sustained deployment will demand the participation of reservists and reserve units on a continuing basis. To illustrate the point, 40 percent of Army Guard and Reserve forces who were in service at any time between the beginning of the Global War on Terror in 2001 and October 2007 have experienced at least one period of active service. This pattern is likely to continue as long as U.S. forces are deployed in significant strength to overseas theaters. Some units most needed for sustained peacekeeping, such as public affairs, military police, and Judge Advocate General, are located primarily in the reserve components.

The increase in utilization of reserve units has had different consequences than those of active-unit deployments. Reservists typically hold civilian jobs. When they are called to active duty, reservists must leave their civilian positions for the duration of their mobilization. Reserve mobilizations thus can affect the incomes of reservists and their families, and can also affect the reservists’ employers.

The large-scale mobilization of reservists for the first Gulf War demonstrated a need to protect reservists’ civilian employment. Accordingly, in 1994 Congress passed the Uniformed Services Employment and Reemployment Rights Act (USERRA) to

update and expand reemployment protection that had been enacted in 1940 in the Veteran Reemployment Rights Act. A key USERRA protection is the right of veterans, reservists, National Guard members, and certain other members of the uniformed services to reclaim their civilian employment after being absent due to military service or training. With few exceptions, employers must reemploy their reservists and afford them the rights and benefits determined by seniority as well as certain other benefits available to employees on furlough or leave of absence. In this way, reservists are not penalized for their absence.

While USERRA provides employment protection for reservists, it does so at a potential cost to employers. If an employer does not replace a mobilized reservist, the employer must either face the loss of the reservist's productivity or reorganize operations to compensate for the absence. If the employer does replace the reservist, the employer may incur various costs of search and hiring, and can be faced with the necessity to terminate the new employee once the reservist returns from active service. Furthermore, the employer may have to pay the financial costs of some employee benefits during the period of the reservist's absence.

In recent years, bills have been introduced in Congress to compensate employers for the presumed costs they suffer from their reservist employees' mobilization. In addition, the Small Business Administration (SBA) has acted to protect the economic viability of small firms that employ reservists. In 1999 the SBA instituted its Military Reservist Economic Impact Disaster Loan (MREIDL) program, which provides loans to small businesses that experienced the loss of key personnel to reserve mobilization. More recently, the SBA initiated a program called Patriot Express aimed at helping veterans, including reservists, establish or expand their small businesses.

## **A. ANALYSIS OF EMPLOYER COSTS**

Although USERRA and VRR have been in effect during a period in which reservists have faced repeated mobilizations, little is known about the extent to which their absences have actually imposed costs on their civilian employers. To remedy this lack of information, the Office of the Assistant Secretary of Defense for Reserve Affairs [OASD(RA)] within the Office of the Secretary of Defense asked the Institute for Defense Analyses (IDA) to conduct a study to help determine the costs that employers

experience. IDA's initial report on this topic was completed in 2004.<sup>1</sup> In its report, IDA developed a taxonomy of the kinds of costs that employers might incur due to their reservist employees' mobilization. The costs included lost productivity and revenue, costs of using remaining employees to compensate for lost productivity, hiring and pay costs for temporary or permanent replacement personnel, and the costs of benefits such as leave and pension contributions while reservists were mobilized.

IDA undertook a limited survey to validate the taxonomy and to learn whether employers had experienced other kinds of costs. The sample for the survey was drawn from a list of small businesses that had received MREIDL loans from the SBA. The IDA team recognized that its sample was non-random in several important respects. First, it consisted entirely of small businesses and was limited to those small businesses that had experienced significant economic impact from the mobilization of a key employee (a requirement for eligibility under the MREIDL program). Second, the sample was not drawn randomly with respect to geographic region, industry, or even type of establishment, as it excluded employers in the not-for-profit and public sectors. Third, the sample was limited to eight firms because of resource and time limitations. Despite its limitations, the survey supported the IDA taxonomy and added some information on the experience of affected employers. Typically, employers experienced short-run costs of hiring, workplace dislocation, and in some cases lost business or reduced revenue. Some businesses took several months (or even years) to return to their previous level of profitability following their reservist's return. A few employers claimed that the value of the SBA loan program was diminished by the requirement for repayment. They ultimately had to bear the costs of the reservist's absence, although they might be able to shift the costs from one time period to another in which they could better repay the loan.

The IDA analysis concluded that a systematic survey of employer costs should be undertaken, using the taxonomy developed in the initial project as modified by the results of the small-scale survey. IDA also examined the types of relief that employers might be offered through public policy if the survey concluded that their costs supported such policies. Depending on the nature of employer costs, appropriate policies might include tax relief, formula grants, or case-by-case indemnification. Each of these approaches would have its own combination of windfall benefits, program costs, and administrative

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<sup>1</sup> Glenn A. Gotz, Colin M. Doyle, Neil M. Singer, and Karen W. Tyson, *Analysis of Employer Costs from Reserve Component Mobilization*, IDA Paper P-3872, February 2004.

costs for both employers and the government. Any recommendations about public programs were deferred pending the results of a systematic survey.

## **B. THE SURVEY OF EMPLOYER COSTS**

### **1. The Survey Instrument**

To develop and administer the survey, OASD(RA) contracted with a professional survey research company, CALLC. The survey researchers worked with the IDA team to design a survey instrument that could provide data on all the potential costs identified in the IDA taxonomy and validation process. Efforts were made to ensure that the survey would meet standards for sample size, response rate, and coverage. The sample was stratified to cover variations of industry, size of establishment, geographic region, and type of establishment (for-profit, not-for-profit, or state/local government agency).

The survey design process proved to be difficult. The design team was concerned about the ability and willingness of employers to provide the requested information, which might have required them to retrieve data from several years earlier. Furthermore, asking about the many different types of potential costs made the survey lengthy and complex. As a result, a two-part survey instrument was designed. Part I addressed the costs of benefits provided to reservists during their absence from the employer: pension, leave, and health costs. The survey also asked employers about the extent to which they provided voluntary support for their absent reservists. Part II addressed workplace costs such as employment of replacement personnel, rearranged workloads, overtime pay, and lost business. Each part of the final survey instrument was estimated to take 20 to 30 minutes to complete. To reduce the burden on respondents, Part I was intended to be completed by an establishment's human resources manager, while Part II was meant to be filled out by a workplace manager.

### **2. Administering the Survey**

CALLC conducted pretests of the survey at several points during the design process in order to estimate the time needed to complete both parts and to obtain feedback from employers about technical issues such as proprietary data. CALLC also fielded a pilot survey prior to full implementation to further test the ability of employers to provide the required information. The pretests and pilot indicated that the completed instrument posed no major difficulties for respondents. Employers generally indicated no aversion to responding to the survey.



To develop a respondent sample, IDA drew on a Department of Defense database: the Civilian Employment Information (CEI) file. This database includes reservists' identification of their civilian employers. The CEI file was not a perfect database at the time of the survey for several reasons. First, it is not comprehensive, although all four military services have increased the percentages of their reservists who have responded to it. Second, it is not necessarily current; reservists are asked to make a one-time identification of their civilian employer, and the information is not often updated. Third, there is no quality control on the data provided by reservists. Nonetheless, the CEI is the only database that exists on the civilian employers of military reservists. IDA first identified military reservists who were called to active duty during calendar years 2005 and 2006. These reservists were then matched with the employers they cited in the CEI, yielding a population of employers who had experienced the loss of one or more reservists to mobilization during 2005-2006. From this population of employers, IDA and CALLC eventually drew a sample of 2,205 employers. Due to the limitations of the CEI, in practice not all of the employers could have been expected to have actually employed mobilized reservists.

For a variety of reasons common in survey research, the survey could not be administered to the entire sample of 2,205 employers. Some employers were misidentified in the CEI. Others could not be linked to business addresses. Some employers may no longer have been in operation. Ultimately, CALLC sent out 1,527 survey questionnaires to employers identified through the CEI. The survey was fielded in the summer and fall of 2007. Despite the length and complexity of the survey, the response rate from the surveyed establishments was very satisfactory. In total, 997 employers returned at least one part of the two-part survey instrument, a response rate of 65 percent. Of the 997 employers who responded to the survey, only 549 said that they had employed reservists who were called to active duty. Some of those who responded to the survey only completed Part I or Part II, rather than both sections. Of the 549 employers aware that their reservists had been mobilized, 478 completed the full survey. Since analysis of the results requires completion of both sections, the survey ultimately produced 478 valid responses.

All of the respondents were drawn from the subset of the CEI consisting of the listed employers of reservists who were mobilized. We cannot determine the reasons that 448 of those employers claimed not to have employed such reservists. It is possible that reservists' identification of their employers in the CEI file may have been out-of-date. It is conceivable that some reservists called to active duty may have resigned rather than

take military leave. It is also possible that the employer personnel who responded to the survey may not have been aware of the mobilized employees, as the survey materials did not include the name of the matched reservist.

## II. RESULTS OF THE SURVEY

### A. EMPLOYER SATISFACTION

Employer responses confirm that military reservists are valued employees. The survey asked employers to evaluate their reservist employees in eight dimensions or characteristics, comparing them in each case to other employees. In all cases the reservists were considered to be equal or superior to other personnel. The data are tabulated in Figure 1. As the data show, employers prefer reservists because they are considered to possess skills generally superior to other employees. In particular, reservists rank high in terms of leadership, teamwork, and dependability, all of which are characteristics related to military training and experience. In all dimensions, the difference between those reservists rated the same as or better than other personnel and those rated worse is highly statistically significant.

The added value that employers see in reservists could motivate them to support their reservist employees, even at the cost of periodic absences for active service. To

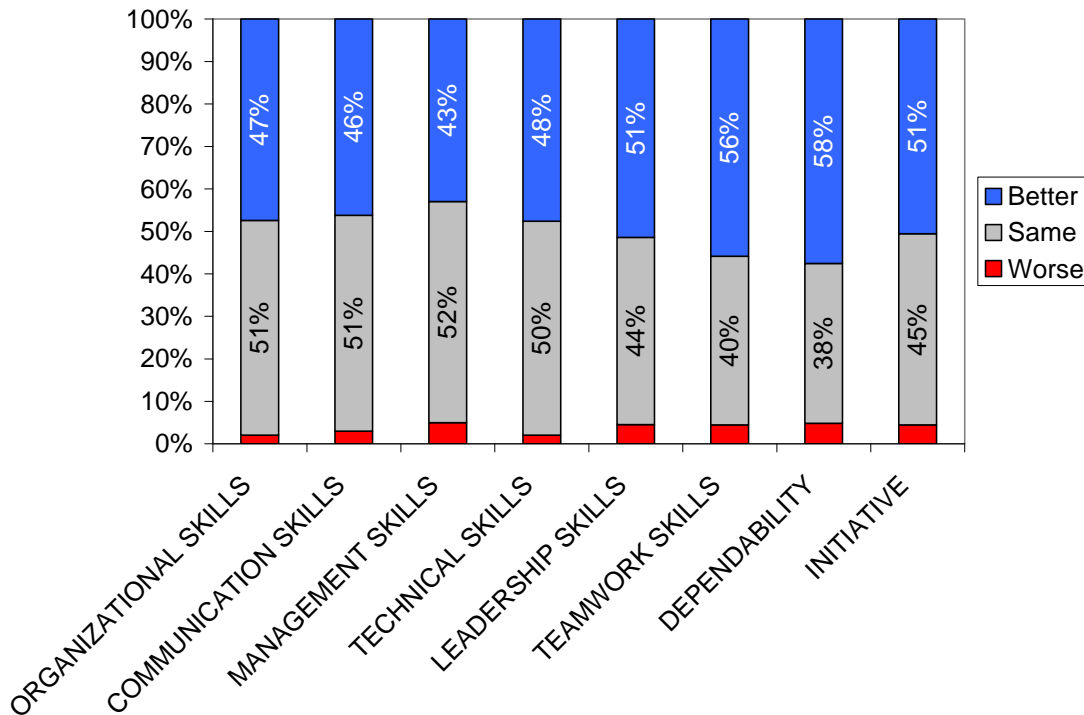
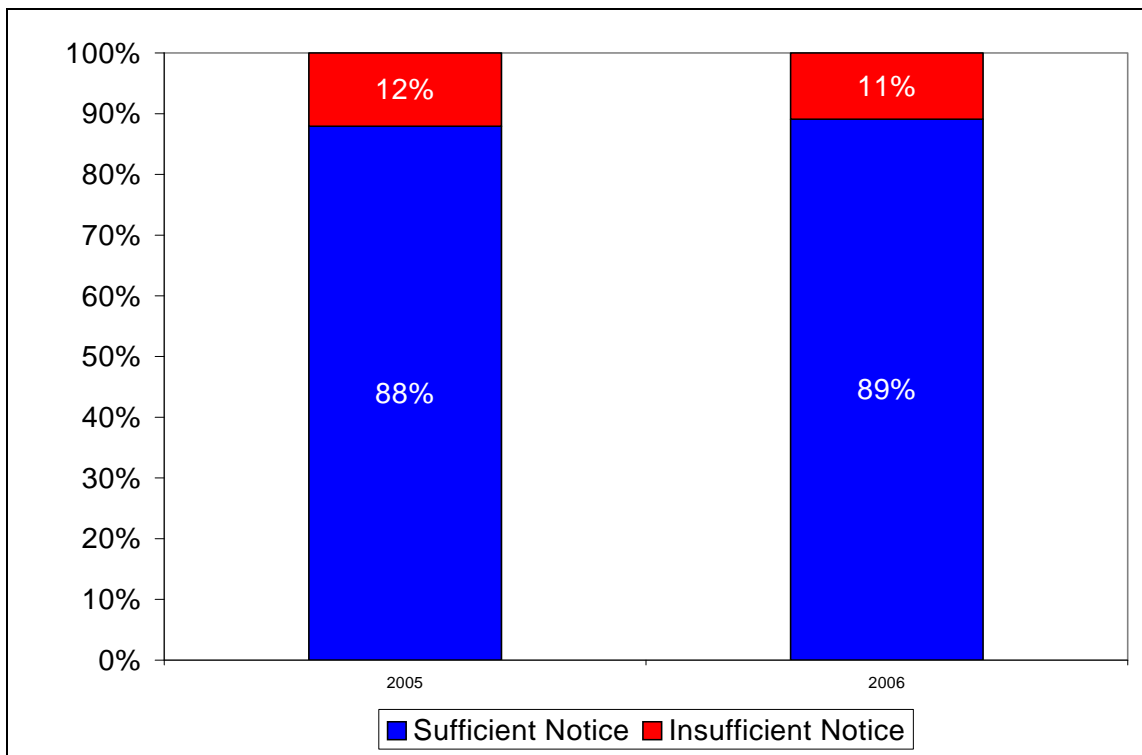


Figure 1. Employers Generally Are Satisfied with Reservist Employees

help employers adjust to those absences, reservists typically are notified at least 30 days in advance of being mobilized. For the most part, employers find this to be an adequate amount of notice (see Figure 2). The difference between the percentage of employers who find the amount of notice to be adequate and those who do not consider it adequate is highly statistically significant. Employers were asked about their experience with reservists who were mobilized in 2005 and 2006. There is no significant difference between their responses for the two years.



**Figure 2. Employers Generally Receive Adequate Notice of Reservists' Activation**

## **B. OVERVIEW OF EMPLOYER COSTS**

Although the survey was designed to permit stratification of the results along several dimensions, the number of completed responses was not large enough to conduct all of the planned analyses. Instead, the sample was only large enough to stratify respondents into four groups: small for-profit firms (fewer than 100 employees); large for-profit firms; private non-profits; and state and local government agencies. Of the 478 complete responses, 172 were from small firms, 149 from large firms, 37 from non-profits, and 120 from government agencies. The survey asked employers about the costs

they incurred separately in 2005 and 2006. Results for the two years are combined in the analysis.

Employers provided data on their costs in several categories. Overall, in every category, the majority of respondents reported no workplace costs from reservist activation. In some cases employers claimed to have gained from activations, typically because they were able to hire temporary replacements at lower pay. Among those firms that reported costs in any category, the costs were modest in most cases and did not differ greatly across the different types of employers. A small number of employers, however, reported very large workplace adjustment costs. These employers were either small businesses or first-responder state and local government agencies. About one-fifth of small firms lost business when their key reservist employees were called to active duty. Limitations of the survey precluded combining these costs with other workplace adjustment costs. The survey also failed to produce quantifiable information on the costs of benefits paid to reservists during their periods of active service; however, those costs appear likely to be modest in most cases.

In addition to these costs, many employers choose to provide voluntary support to their activated reservists or their families. These types of support, while not mandatory costs of reservist mobilization, nonetheless provide a significant indication of the value that employers place on their reservist employees. The survey data on voluntary expenditures are tabulated later in this analysis.

### **C. WORKPLACE ADJUSTMENT COSTS**

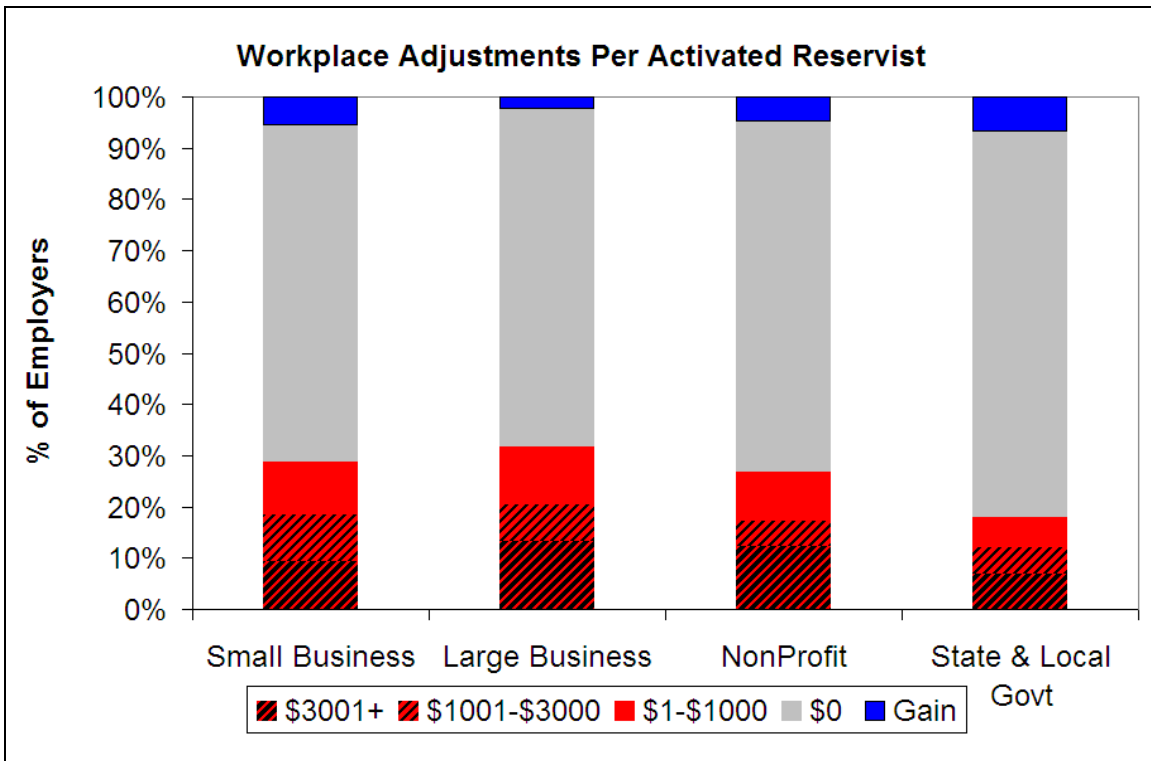
Employers were asked about several different kinds of workplace adjustments, based on the taxonomy developed in previous IDA work. One way for employers to compensate for the absence of a reservist employee is to *retrain other personnel*, in which case they would incur costs of retraining. Another possibility is to handle additional workload by paying *overtime costs* to other employees. If additional personnel are needed, an employer might *hire temporary replacements*, or—if the nature of the job is such that temporary personnel are not an option—*hire permanent replacements*.<sup>2</sup> In either event, the employer might incur *costs of search and hiring*, such as employment agency fees, *training costs*, and *differential wage costs*, reflecting the difference in pay between the absent reservist and the replacement. In some cases, replacement personnel

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<sup>2</sup> In the earlier IDA study, some employers were forced to hire permanent replacements because their activated reservists were skilled professionals for whom temporary replacements could not be found.

might be paid less than the reservist, leading the employer to derive a gain from the reservist’s mobilization.

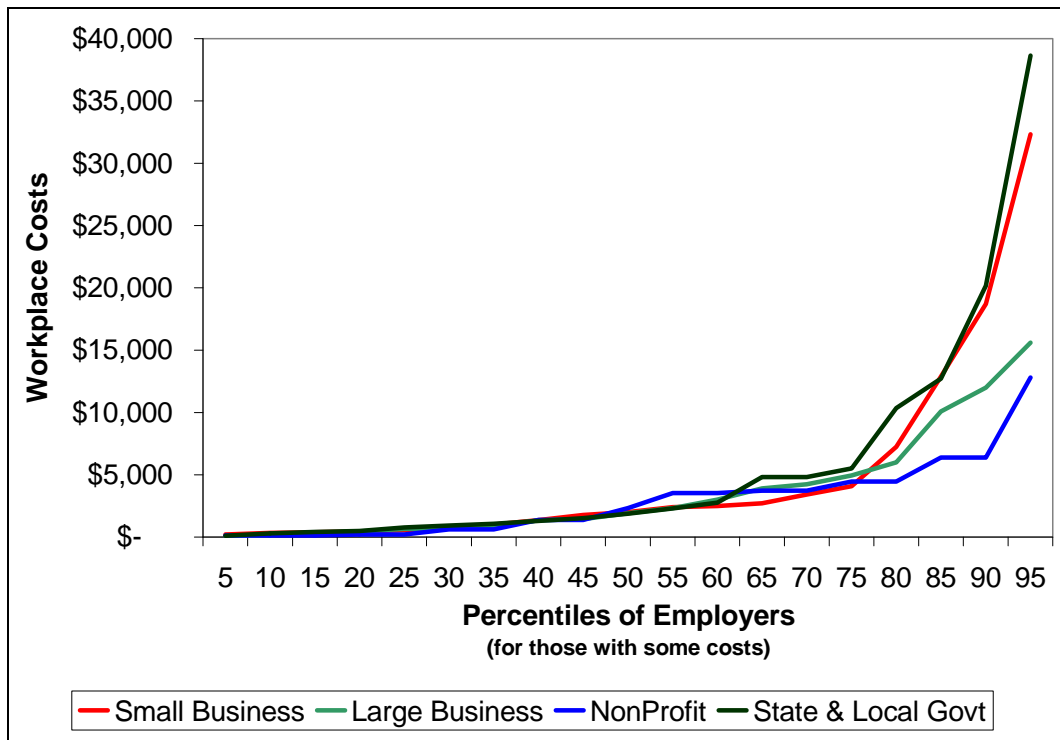
The totals of all these costs reported by employers are tabulated in Figure 3. In each category of employer, the majority of respondents reported no costs from reservist activation. A small number—less than 10 percent—actually derived gains from reduced salary costs. Between 20 percent (state and local government agencies) and 35 percent (large for-profit businesses) of employers reported net costs of workplace adjustment. For those reporting net costs, the median cost varied between \$2,320 (for non-profit establishments) and \$1,880 (government agencies), with small businesses at \$2,001 and large businesses at \$1,920. Fewer than half of these affected employers had costs over \$3,000 per reservist. The data tabulated in Figure 3 are the costs experienced over the entire period of the reservist’s activation; therefore, most of the affected employers had workplace adjustment costs of no more than a few hundred dollars per month over an 11-month mobilization period—the average for reservists.<sup>3</sup>



**Figure 3. Most Employers Have Little or No Costs of Workplace Adjustment**

<sup>3</sup> Activations for FY2002 through FY2006 averaged across all services.

A relatively small minority of employers in each category experienced much larger costs from reservist activation. The distribution of cost-incurring employers in each category by the level of workplace costs is shown in Figure 4. In every category, 95 percent of employers had workplace costs of less than \$5,000; however, costs for the other 5 percent—or 15 percent of those with some costs—were in some cases much greater. In particular, some small businesses had costs of over \$30,000, and some government agencies’ workplace costs approached \$40,000. Every one of the severely affected government agencies was a first responder, such as a police department or emergency medical team. The main reasons for their high costs were in training and the payment of overtime to remaining personnel. (In addition, some first responder agencies, like many other state and local government agencies, elect to continue paying at least partial wages to their activated reservists. Such payments, however, are voluntary and do not constitute costs of workplace adjustment.) In the case of the severely affected small businesses, the principal reason for their high costs was the expense of training employees to do the jobs of the mobilized reservists.

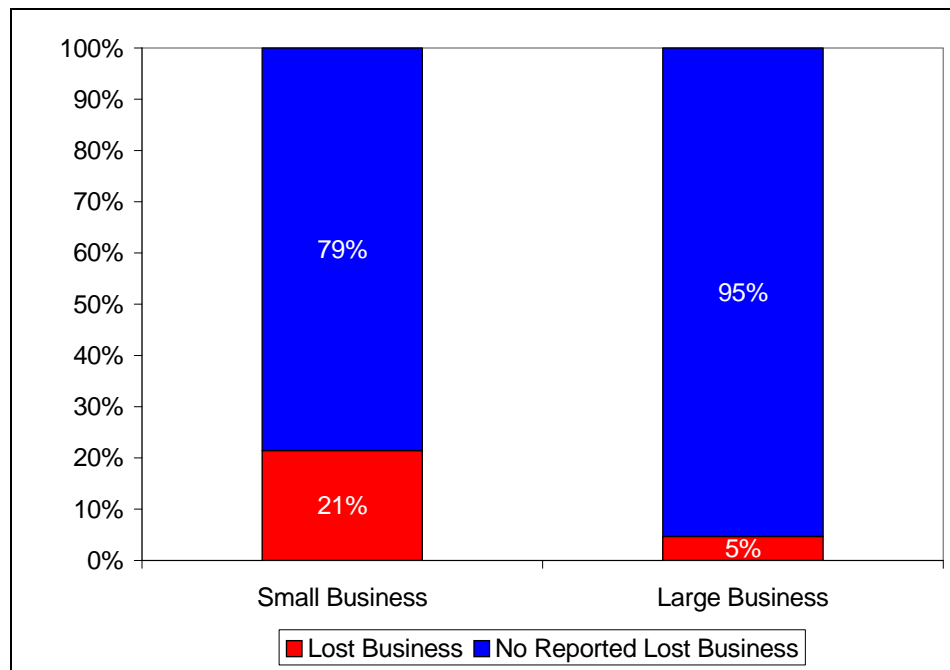


**Figure 4. Some Employers Had Very Large Workplace Costs**

## D. LOST BUSINESS

IDA's preliminary study of employer costs suggested that losing business was a common consequence of reservist mobilization among small businesses. Loss of a key employee might mean reduced marketing, diminished productivity, the inability to seek large-scale jobs, or shifts in a firm's output.<sup>4</sup> Some of the respondents to the earlier survey reported that they had been driven out of business by their reservist's activation.

Designing survey questions to ask employers about lost business proved difficult. Part of the difficulty related to terminology: Did the firm lose revenue, profit, gross receipts or sales? Another issue related to identifying the baseline used to calculate the loss of business. In the end, the study team decided to raise the issue of lost business as an open-ended question, in effect letting employers decide what the appropriate definition was and how much they were affected. The results of this question are tabulated in Figure 5.



**Figure 5. Some For-Profit Employers Lost Business from Reservist Activation**

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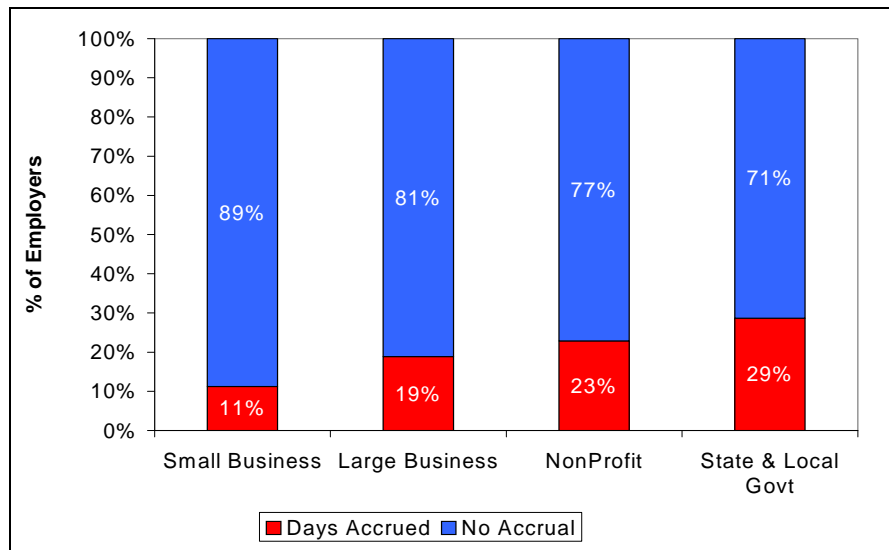
<sup>4</sup> For example, one medical partnership surveyed in the earlier study had to reduce its workload of surgeries and substitute patient consultations and physical therapy when one of its surgical partners was called to active duty.



While only a very small percentage of large firms reported any loss of business, more than 20 percent of small businesses did so. Not surprisingly, given the open-ended nature of the question, the amounts claimed to have been lost varied greatly, from as little as \$25 to \$1 million. The wide variation suggests that employers may have used different concepts of lost business and that some may have suffered severe losses in some instances.

**E. BENEFITS FOR RESERVISTS**

USERRA mandates that employers provide some benefits to reservists during their absence for active duty. In practice, however, the USERRA mandates impose fewer costs on employers than might appear to be the case. The principal kinds of benefits paid by employers include pensions and leave (annual, sick, or family). USERRA requires that employer-provided health insurance benefits be continued only for reservist absences of 30 days or less. Reservists on active duty for more than 30 days are covered by the military’s health care system for active personnel, and a reservist’s family is eligible for TRICARE coverage while the reservist is on active duty. Some employers choose to continue health care coverage for their activated reservists, but that is a voluntary expenditure rather than a cost of mobilization, although an employer may require a reservist employee to pay up to 102% of the cost for continuing the employer-sponsored health care plan. Similarly, USERRA requires that employees continue to accrue leave during their period of active service, but only if their employer provides leave accrual for employees who are “on furlough or leave of absence.” The impact of USERRA on leave accrual is shown in Figure 6.



**Figure 6. Some Employers Incur Costs of Leave Accrual during Activation**

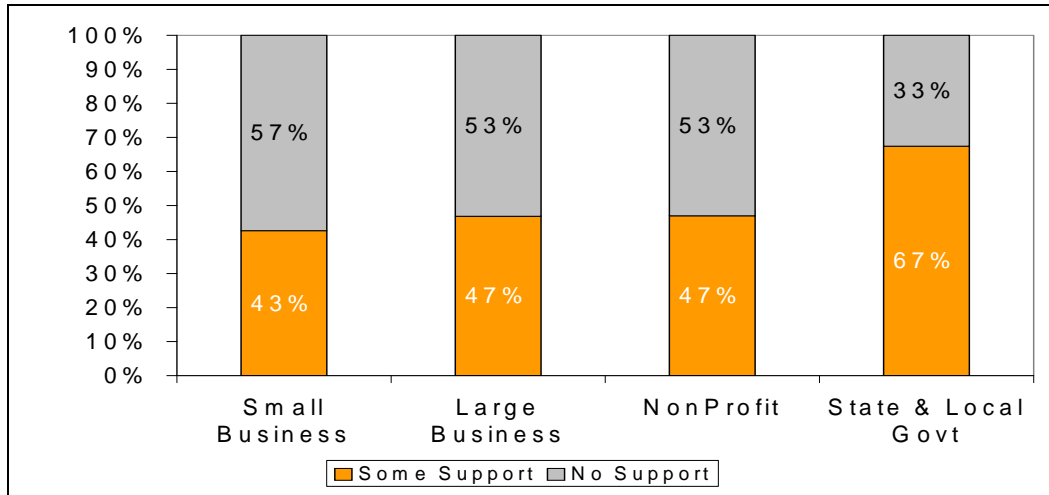
Pension costs may also impose less of a burden on employers than USERRA would appear to mandate. Most retirement plans in the private sector are contributory, requiring contributions from the employee. USERRA requires employers to provide accruals for their absent reservists only if the reservist also makes a contribution. Reservists need not make contributions during the period of activation, but may make them up upon return from active duty; employers are then required to make up their contributions. National data suggest that pension costs associated with reservist mobilization are not excessive. In 2003, for example, only 35 percent of employees in small businesses participated in a pension plan. Sixty-five percent of employees in large businesses participated in 2003; 98 percent of state and local government employees participated in 1998. The average cost to employers for pension plans is about \$1 per hour worked for private employers, and \$2.50 per hour for state and local governments. Thus, the monthly pension costs to employers for reservists who participated in their pension plans and made full contributions upon their return would be about \$430 for private firms and about \$440 for state and local governments. The cost of pension accrual would be about \$4,800 for an 11-month activation of a participating employee.

The employer survey included questions about pension costs; however, the responses were difficult to interpret and proved to be unusable. Issues arose because some survey questions proved to have multiple interpretations. First, employers were asked if they made contributions to a defined benefit plan, *and* if they made contributions to a defined contribution plan. CALLC was able to eliminate the ambiguities in these responses; however, many employers contributed to both kinds. Second, questions regarding the contribution rates for defined contribution plans elicited ambiguous results that prevented us from distinguishing employer contributions from those of employees. Third, employers were asked what amount they contributed to a plan upon the reservist's return; some of this data was reported as monthly amounts. It is unclear whether these numbers were the monthly accumulations during activation that the employer was required to make up, or were new contributions that simply restarted on the reservist's return.

## **F. VOLUNTARY SUPPORT**

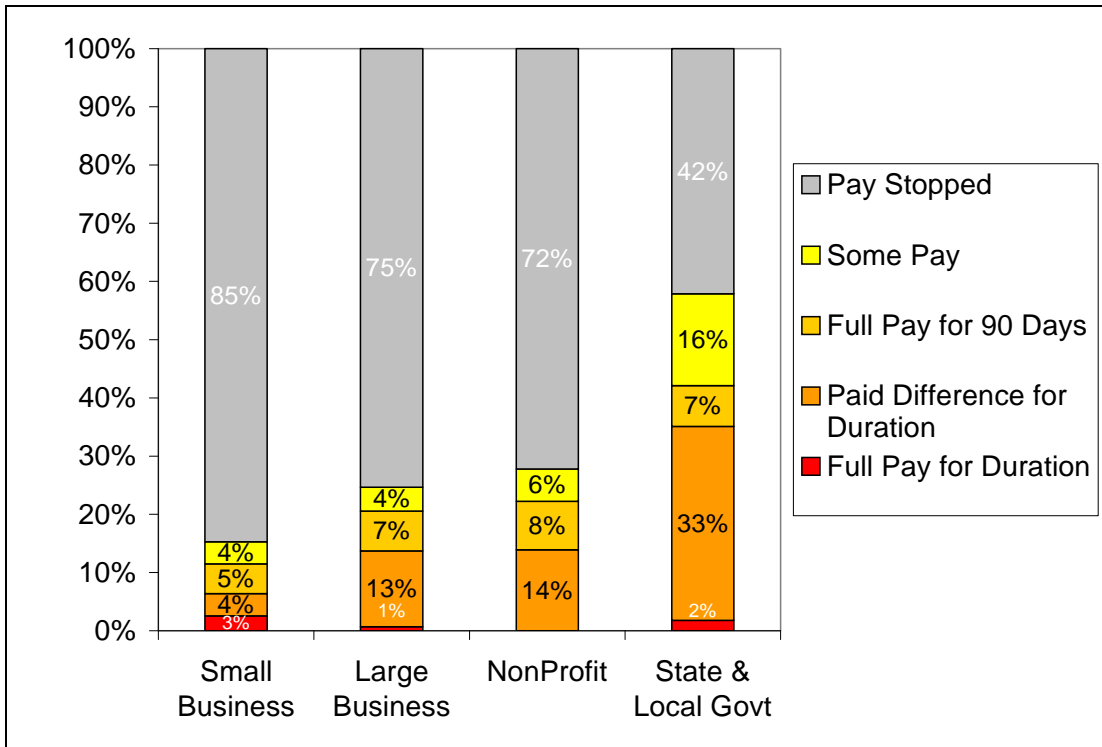
A significant percentage of employers chose to provide some amount of voluntary support for reservists called to active duty and their families (see Figure 7). In some cases this support took the form of continuing health care benefits for reservists' families, allowing them to continue to use their family medical care providers without going

through the unfamiliar mechanisms of TRICARE. Some employers provided other forms of in-kind support for reservists and their families such as care packages, phone cards, laptop computers, home repair and in a few cases making car loan and mortgage payments (see Appendix A for a breakout of these kinds of support).



**Figure 7. Many Employers Provide Voluntary Support for Activated Reservists**

The most common type of voluntary support was the continuation of some portion of the reservist’s pay while on active duty. Such support can range from continuing the reservist’s full pay for the duration of his mobilization, continuing pay for some period such as 30 or 90 days, to making up the difference between military pay and civilian pay, or a combination of these approaches. The distributions of the types of voluntary pay support are shown in Figure 8. The most common practice in each category is to stop the reservist’s pay upon mobilization. Over half of state and local government agencies elect to provide some form of pay support. Twenty-five percent or more of large businesses and non-profits also provide pay. Small businesses generally appear to be less able to provide pay support.



**Figure 8. Many Employers Provide Continuation of Pay for Activated Reservists**

### **III. IMPLICATIONS FOR PUBLIC POLICY**

In recent years, several bills have been introduced in Congress that would provide some form of relief to employers of activated reservists. The Hope at Home Act, S. 1142 in 2005, proposed a tax credit to employers who paid differential wages to their activated employees. The credit would be 50 percent of the wage costs. The Patriot Employers Act, S. 1945 in 2007, proposed a 1 percent income tax credit for employers meeting several criteria of a “Patriot Employer.” The Eagle Employers Act, H. 5907 in 2008, made a similar proposal. However, no data was available on the magnitude of employers’ costs and how many employers experienced them. Policy proposals were formulated without a complete picture of the problem they were intended to address. The survey of employer costs provides the first systematic data on the nature and extent of the problem. In light of this new data, cases can be made both against and for the use of public policy to relieve affected employers.

We cannot aggregate the different elements of employer costs into a total cost for any employer or group of employers due to limitations in the design and implementation of the survey. The survey provides detailed data on workplace costs and voluntary contributions. We cannot quantify costs due to loss of business. We have broad estimates of benefit costs, but these are not derived from the survey and are not specific to employers with activations.

Nonetheless, the magnitudes of reported costs, and the finding that only a minority of firms in any category experience costs, offer some guidance in considering whether employer costs should be targeted by public policy remedies, and in choosing among different policy options. First, the data indicate that only a minority of employers experience costs from mobilization, and even among those who suffer costs, only a much smaller minority are severely affected. Second, the survey data suggest (although they do not demonstrate) that employers’ costs may be greater than the study team was able to tabulate. In addition to the tabulated workplace costs, some small businesses reported costs from reduced sales, revenues, or profitability. The survey questions regarding employee benefits suggest that some employers may incur costs from accruals of these benefits, especially pension contributions. Furthermore, many employers choose to make voluntary contributions to support their reservist employees during their periods of active duty. Although voluntary support is not a mandated employer cost of mobilization, it

may affect both employers' attitudes toward employing reservists and reservists' willingness to return after completing active duty.

Finally, the data suggest that some reservists may be reluctant to notify their employers of their reserve affiliation. The high proportion of employers who responded that they did not employ activated reservists, despite the fact that the survey sample was drawn from a list of employers who did employ them, indicates that some employers may not be aware that some of their employees are reservists. A reason for this might be that reservists fear some form of penalty or sanction from employers despite USERRA protections. If that is the case, an indemnification program might be of value in improving reservists' employment conditions.

#### **A. THE CASE AGAINST POLICY REMEDIES**

There are both theoretical and practical arguments against compensating or indemnifying employers for the costs associated with reservist activation. We offer four theoretical arguments. The first and most compelling theoretical argument is that reservist absences are simply a risk or an expected cost to an employer. Employers must incorporate that risk, like any other business risk, in their business decisions. In fact, reservist absences have become predictable given the pace of mobilizations and deployments after 2003; consequently, employers should be able to incorporate expected absences in their business planning. According to this argument, indemnifying employers for the costs of activation is unnecessary and would simply confer windfall gains on good planners while bailing out bad ones.

Second, there is no guarantee that a policy of indemnification would provide any benefit to reservists themselves. The objective of public policy in this area should be to offer employers an incentive to employ reservists and to discourage employers from penalizing or discriminating against them. However, benefits for employers would only be loosely related to reservists' employment because many reservists have not been, and are unlikely to be, subject to activation. Moreover, any broad policy of indemnification would fail to relate benefits to employers' own costs, and thus would not provide direct job protection.

Third, it is not clear that any policy remedies are actually needed to protect reservists. As the data tabulated in Figure 1 show, reservists generally are attractive and successful employees. If some employers are disadvantaged by reservist activation and reduce their employment of reservists, other employers could be expected to be eager to

hire them. Thus, the demonstration that some employers incur costs need not have any impact on overall reservist employment.

Finally, any need for new policy remedies is diminished by the existence of the SBA MREIDL loan program. Another SBA program, Patriot Express, provides guaranteed loans to veterans who own small businesses. If a business is truly disadvantaged by reservist activations, the SBA programs offer interim financial support to help it adjust and remain in operation. Businesses that cannot repay loans could be those that are not viable in the long run and would be forced to close, which would result in the reservist having to find other employment.

There are also practical reasons why policy remedies may be undesirable. The data show that only a minority of establishments report any costs at all from reservist activation. Therefore, under any broad-based policy two-thirds of all recipients would be compensated for costs that they did not actually incur. Moreover, the costs that employers do incur vary widely. Any policy that established a single indemnification rate would be inefficient because it would undercompensate some employers and overcompensate others. These considerations argue against the kinds of programs that have been proposed in draft legislation to address employer costs. Still, a practical argument can be made against any programs tailored to the experiences of individual employers. Any program that compensated employers for their actual costs would be expensive to administer. The amount of aid would have to be determined on a case-by-case basis. Such a program would also have definitional issues about what costs qualify for aid, and in what amounts.

The preceding discussion is couched in terms of for-profit businesses; however, it also applies to non-profits and even to state and local government agencies. These employers can anticipate reservists' activations and plan for overtime, reduced productivity, and other effects of their absences. The majority of those employers report no costs and thus are not in need of indemnification or other policy remedies. Across-the-board programs would be as inefficient for non-profits and state or local agencies as they would be for other employers.

## **B. THE CASE FOR PUBLIC POLICY**

Each argument that can be raised against the need for remedial policy can be countered with an argument in favor. The claim that employers should internalize the risk and cost of reservist activations demands a level of knowledge and certainty that does not exist in practice. Even if they anticipate that their employees will be activated,

employers do not know when the mobilization will occur, for how long the employees will be absent, or what the business workload will be during that time. Therefore, reservist activations impose costs that are difficult for employers to estimate and anticipate. In this environment, employers may have a consistent bias against employing reservists. The advantages that reservists provide might overcome some of that bias. However, reservists would tend to be underemployed or underpaid compared with what their personal characteristics and productivity would otherwise command. Despite USERRA protections, employers can find ways to protect themselves against the costs that reservist employees impose. For example, they may limit reservists' promotions, demand that they relocate or change their job descriptions. Indemnifying employers for those costs is one way to provide relief and could further serve as a financial inducement to hire reservists.

The SBA's programs do not fill the need for addressing the effects of mobilization. Businesses that receive loans eventually have to repay them and thus incur costs that other competing employers do not incur. Even if the SBA's loan terms are favorable, they can affect liquidity, cash flow, and a business's ability to compete. Affected employers may be unable to remain in business, leaving no job for the reservist.

The need for policy remedies cannot be dismissed on the grounds that only a minority of employers of any type actually experience costs from mobilization. Reservist activations have a disparate impact both across categories of employers and within categories. In particular, small businesses have greater costs than large ones, and are more likely to suffer lost business. Among government agencies, first responders face the highest costs of activation. Residents of states or localities whose first responders are subject to mobilization must pay higher costs or experience losses in service. Thus, the burden of military mobilizations upon employers and taxpayers is imposed unequally.

### **C. POLICY OPTIONS**

Three kinds of policy remedies can be considered: tax credits, liberal loans and grants. Each poses problems in terms of its effectiveness, dollar cost, administrative complexity and impact upon recipients. Tax credits are the simplest option. A program could be designed to offer a fixed dollar credit for each month that an employer suffered the absence of a mobilized reservist. Such a program would be simple to administer, as it would add minimally to the cost of preparing or auditing a tax return. The dollar cost could be fixed at any level; a reasonable amount based upon the survey data could be of



the order of \$700 per month. To include beneficiaries with no net tax liability, the program could be designed with a negative tax feature.

Two drawbacks arise with this program. The first drawback would be its inefficiency. To minimize the administrative burden, there would be no need for an employer to document that it had actually incurred costs. However, as the data show, over two-thirds of all benefits would go to employers who did not incur costs, and among those who did incur costs, the amount of the credit might not fully defray those costs. Very few employers would actually experience costs equal to the credited amount. The second drawback is that a tax credit would exclude many employers who incur significant costs: non-profits and government agencies. This issue is especially pertinent for government agencies, including the first responders that the data show are the most severely affected agencies. Under the tax credit approach, these agencies would receive no benefit. The people they serve either would face degradations in service or would pay higher taxes to maintain the level of service prior to reserve mobilization.

Loan programs offer a different set of advantages and disadvantages. The greatest advantage of business loans is that they already exist in the form of SBA programs, and that the SBA has developed the capability to administer the programs. A loan program would be much more efficient than tax credits, as only those employers who could show costs would be eligible for loans. Therefore, a loan program would probably pay out less money overall, reducing the cost of the program.

There are nonetheless several drawbacks with this approach. First, loan programs would have high administrative costs for the government and high application costs for employers. Employers would have to document their costs and comply with other application procedures. Second, one criterion for eligibility may exclude affected employers; for example, the MREIDL program requires that the activated reservist be a "key employee." Third, the SBA's program by definition is restricted to small businesses. Although a broader loan program could include other employers, such as non-profits, a loan program would be unlikely to benefit first-responder agencies that are hardest hit by mobilization. Finally, a loan program is subject to the criticism that it only defers the costs that employers incur. Such a program would thus fail to correct the inherent inequities in reservist activations. Because the loan is only a transitory benefit, the cost of obtaining it might easily be greater than its value to the employer.

A third approach to indemnifying employers would be to offer grants to offset the costs they incurred from mobilization. The advantage of a grant program is that if limited

to severely affected employers, it would be an efficient use of public funds. It would be targeted to protect and encourage reservists' employment. A grant program could also be offered to non-profits and even to state and local government agencies. The major drawback of such a program is similar to that of a loan program: Grants would be administered on a case-by-case basis and would impose high administrative costs on both the government and applicants. Regulations would have to be drawn to protect the government from fraudulent applications, as the absence of a repayment provision would give employers a strong incentive to apply.

#### **D. CHOOSING BETWEEN POLICY OPTIONS**

Policy-makers must determine the necessity of indemnifying employers' costs from reservist mobilization. On the one hand, the drawbacks of all of the public policy options may well outweigh their advantages and the costs to employers may be deemed to be less onerous than the costs to the taxpayer associated with an indemnification program. On the other hand, if policy-makers decide to pursue employer indemnification, the study team concludes that a limited, controlled grant program targeted at employers who experience severe costs would be the best option. Such a program would focus most directly on the employers who are harmed by activation. Grants would be of greater value than loans to employers and thus would offer the greatest likelihood of protecting reservists' employment. Grants would avoid windfall gains for employers who did not incur costs, and would come closest to matching the benefit to the costs actually incurred. The administrative costs of applying for grants could be sufficient to dissuade applications from employers who experienced only minor costs.

The study team envisions such a grant program as supplementing the loan programs currently available through the SBA. The SBA's experience with its loan programs could provide a model for developing a grant initiative. In order to ensure that the grants were given to the most severely affected employers, criteria would be established for employers to document their costs. Grants would be limited to the amounts that the employers could document in order to ensure the program's efficiency, reduce the administrative cost to the government, and reduce the program's overall dollar cost. To address the higher costs reported by state and local government first-responder agencies and promote public safety and health care, the grant program could include a dollar amount earmarked for first responders. These applicants would still be required to document the extent of their costs, but fast-track procedures could be implemented to help agencies meet their staffing and coverage needs.

## IV. CONCLUSIONS

The Employers Economic Impact Survey presents data, for the first time, on the extent to which employers of reservists are affected when their reservist employees are called to active duty. The survey shows that only a minority of employers in any category experience costs. For those who do, costs of workplace adjustments usually do not exceed a few hundred dollars per month during the reservist's absence. Overall costs to employers may be greater due to lost business, personnel benefits, and voluntary expenditures. However, few employers appear to be severely affected by reservists' activation.

An argument can be made that public policy should take cognizance of the minority of employers who experience considerable economic losses. The available public policy approaches include tax credits, loans, and grants—each of which offers advantages and drawbacks. The objectives of public policy should include reducing the possibility of adverse effects on reservists' employment, holding down administrative costs, and focusing benefits on those employers who need them most. Among the public policy choices, the study team concludes that a grant program that is tailored to apply only to employers who can demonstrate substantial losses offers the greatest promise of achieving these goals.

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**APPENDIX A**  
**INCIDENCES OF NON-PAY SUPPORT**

<b>All Employers</b>	<b>Percentages</b>
Continued Health Coverage	22.3
Care Packages	18.1
Technology (Laptops, Web Cameras, Etc)	4.2
Phone Cards	3.4
Home & Yard Repair	3.4
Gifts	2.7
Unspecified Help To Family	2.5
Monetary (Donations, Bills, Etc)	2.3
Letters/Emails	1.9
Other/Not Described	1.9

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## **APPENDIX B**

### **GLOSSARY**

ASD(RA)	Office of the Assistant Secretary for Reserve Affairs
CEI	Civilian Employment Information
EEIS	Employers Economic Impact Survey
IDA	Institute for Defense Analyses
MREIDL	Military Reservist Economic Impact Disaster Loan
SBA	Small Business Administration
USERRA	Uniformed Services Employment and Reemployment Rights Act

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