Wealth COACH

Financial planning is different for members of the military. Here's what you need to know

By Jeanne Sahadi, CNN Business
Updated 12:41 PM ET, Thu November 11, 2021

If you're in the US military, there are many potential financial benefits available to you and your family -- even if you serve for just four years.

For instance, there's some tax-free compensation, generous educational benefits, zero-to-low-cost health care, housing allowances and a host of free services on base.

But your financial life is also likely to be upended a few times due to multiple deployments, relocations to other bases, and your transition back to civilian life when you leave the military, or even just transition into the Reserves or National Guard.

That's why certified financial planners who counsel military and veteran families suggest you anticipate and plan for what's coming down the pike so you can minimize financial disruptions and still build savings over time.

"You have to get good at managing cash flow as you go to drastically different locations. It's like starting over every two to four years," said Adrienne Ross, a certified financial planner in Washington state whose husband served in the Air Force.

By that, Ross means your income, taxes and living costs (like childcare and housing) can change a lot from one place to another -- especially when you live overseas for a few years and then return to the United States. So, too, can job opportunities and income potential for your spouse if they work in a field that requires state-issued professional licenses.

Here are some key areas she and other planners say are important to navigate carefully if you want to maximize your financial security.

Related Article: 10 ways to honor veterans beyond Veterans Day

Divide your money across buckets

To help manage cash flow and stay out of debt throughout your military career, Arnie K. Cabiles, a certified financial planner in California who also counsels members of the Marine Corps in Hawaii, recommends allocating your pay across five different categories.

The first bucket is for monthly bills. The second is for emergency expenses, such as an unexpected trip back home to see a sick family member, or a costly repair if your car breaks down. The third is for reserve funds to pay occasional bills, such as insurance premiums due every six months or an anticipated home repair. The fourth bucket is for investments in a taxable account dedicated to your mid-term goals, such as saving for a down payment. And the fifth is for retirement savings, much of which will be automated through the military's Thrift Savings Plan (see below).

Weigh the risks of buying a home

The temptation to buy a home -- especially when you have a young family and want to feel settled -- may be hard to resist, especially if you qualify for a VA loan, for which you don't have to put any money down and can roll into your loan an additional 3% for closing costs.

But here's the problem: You start life in your new home owing more to the bank than the house is worth.

That may still be a workable solution, but only if you're sure you will stay in that home for at least five to seven years, which is unlikely for many military members.

If you leave sooner, and your home doesn't sell for as much as you bought it, you will owe money to the bank. "That's because, in the first five years, you're paying mostly interest so you don't have time to build equity and cover the cost of selling," Ross said.

Or you might have a hard time selling your home at all, in which case you may resort to renting it out. Again that might work for you financially, but only if the rent you can charge covers your mortgage. Plus, you'll want to be comfortable with the idea of being a landlord.

If you expect to move in a year or two, and you have young children, you'll face a whole new matrix of childcare arrangements and costs in your new locale.

"One person in Alaska had their childcare all set up but then moved to Virginia, where the cost basically tripled," Ross said.

While military families can apply for free childcare or cost assistance on- and off-base, they may have to pay out of pocket for the childcare they need in the meantime while they wait for their applications to be approved.

Related Article: Jill Biden and Elizabeth Dole team up to highlight military caregiving

That's why Ross suggests clients set aside small amounts every month just to cover the money they'll need to pay before their childcare benefits kick in at a new location. "Create a fund to bridge the gap," she said.

Anticipate sticker shock with health care costs

One of the most frequent shocks for people who plan to transition out of the military is just how much they will have to pay for health care coverage, Cabiles said.

"During their time in the service, they will be covered by TRICARE, and pay either nothing in premiums or a very low amount," Cabiles said.

And when service members in their early- to mid-20s decide to leave the military to go back to school or get a job in the private sector, he noted, "the general attitude toward getting health insurance is, 'I don't need it.'"

So he reminds them that a trip to the emergency room can happen to someone at any age and will cost far more if you're uninsured than if you pay a monthly premium and deductible.

If they're in their early 20s, he also reminds them that they can be covered under their parents' health insurance plan until age 26.

Retirement is about choice, not old age

Cabiles has found that his message often doesn't get through when he's advising young service members to save for a retirement that they think of as decades away.

So instead, he encourages them to think of the long-term portion of their savings as a means of "making work optional."

Or, put another way, "Early savings buys your future self a lot of choice," said Brian O'Neill, an Air Force veteran who is now a certified financial planner in Florida.

Under the military's blended retirement system, which applies to those who joined the military after January 1, 2018, you still will qualify for a pension if you serve 20 years -- and it should cover roughly 40% of your military pay starting about a month after you leave the service, Cabile said.

But even if you don't serve long enough to get a pension, 5% of your paycheck will automatically be deducted and invested in the government's Thrift Savings Plan. That is, unless you actively opt out, which Cabiles does not recommend. The government will contribute an additional 1% of your basic pay to your TSP account. But that match won't vest until your 25th month of service, at which point the government will bump up its match to a full 5% of your basic pay going forward.

For those who can afford to do more, which is most likely the higher your rank and the longer your service, O'Neill recommends first contributing enough to the TSP to get a match. Then contribute to an IRA -- which allows annual contributions up to $6,000 per spouse.

Related Article: We asked, you answered: The best financial advice you ever got

Strategize for taxes

Depending on where you're assigned versus where your home state is, you may or may not have to pay much in income taxes. For those times when you don't, factor that in to how much more you can save.

"Most states don't tax active duty military pay as long as you're not serving in the state. So California won't tax you if you're serving in Virginia. But it will if you're serving in California," O'Neill said.

And then of course it may be that your home state doesn't have an income tax to begin with -- such as Texas or Florida.

Or, if you're stationed abroad, a portion of your compensation may be tax free in some locations, Ross said.

Know your options

Whether you're an active-duty, National Guard or reserve service member, a good place to learn about the benefits and financial counseling available to you is the Department of Defense's Office of Financial Readiness site.

Another valuable source of information on your base is anyone in the ranks who has been trained as a command finance specialist -- or what Cabiles calls the "paramedics" of financial planning who can offer quick assistance on an urgent question but then direct you to other resources for more substantive help.