

STATEMENT BY:
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To the Honorable Chairman and Distinguished Members of the Subcommittee:

The American Logistics Association (ALA) is pleased and honored to appear before you today. For over 90 years ALA has worked to promote, protect and enhance the military resale and quality of life benefits on behalf of our members and the military community. And, we are pleased to come before you with our fellow advocates of the military's resale program.

Under the leadership of Mr. Rick Page, of Coastal Pacific Distributors and Chairman of the Board, the ALA is proud to represent America's leading manufacturers, numerous brokers and distributors, service companies, media outlets and other members who are actively engaged in providing goods and services to our Military business partners including the Coast Guard, and the Veterans Canteen Service.

ALA member companies have a huge stake in the well being and viability of the exchange and commissary system. For commissaries, we represent 90 percent of the supply chain all the way from manufacture to distribution to stocking shelves in the stores. Our presence in the supply chain for the exchanges is substantial as well. And, we provide the system with in excess of \$500 million in annual in-kind and direct support.

Mr. Chairman, you can be proud of the system that has been created, embraced and fostered by this Committee. It's a system that works and has served the military, the DoD and the Nation well. As I appear before you today, the vast network of commissary, exchange and MWR programs is providing millions of military personnel and their families with vital American-made products and services. Tens of thousands of dedicated folks are reporting to work to make sure our military are taken care of. And the benefits of this program are well known to you and have been documented by ALA and other advocates.

Chairman Thornberry and members of this Committee have consistently said that the funding levels for defense should be driven by strategy and not the other way around. As a subset of National defense, this translates directly for resale programs as well. Resale reform strategy needs to be laid in before cuts. Any reductions to funding must be predicated on a coherent and deliberative plan that is subject to the same rigid and consistent oversight that has been traditionally practiced by this committee. If reductions are placed ahead of the plan, DoD runs the risk of upsetting and dismantling a carefully designed on base commerce ecology that won't be able to be reconstructed and we believe that the troops, their families, the taxpayer--and the DoD--will pay a heavy price for any precipitous action.

We are grateful to the Committee for fully funding these programs in fiscal 2016. Mr. Chairman, we know that DoD has been under pressure to find savings despite the successive series of relief measures to the DoD top line. There is pressure within the Pentagon and within the Congress to identify areas of waste where funding can be freed up for direct combat readiness expenditures. We get that. In fact, we got it way before most people in this town did. And, that is why the resale system has been consistently and steadily working over the years to reduce costs.

Any objective observer could see that commissary funding has dropped in real dollars nearly 40 percent with nearly \$600 million in annual costs taken out of the program. Exchanges continue to streamline their operations and reduce reliance they have on appropriations—appropriations that are vital to maintaining their global mission and their ability to finance on-going operations and funding for MWR programs. The list is long and well documented in ALA's economic report on resale. It's a model of a working public private partnership where our industry today contributes nearly \$500 million in support and services to our resale partners. It provides some \$4.5 billion in annual savings to patrons. Patrons have invested nearly \$12.5 billion in capital improvements over the years and hold major shareholder equity. It provides vital services for forward deployed forces, DoD school lunches, and a wide range of other

government support functions. And, it provides vital, base-to-base transferable employment to tens of thousands of military family members.

The merits of the system are well known to Congress and especially this committee. The House Armed Services Committee has led the way in enacting a series of measures that were carefully designed to construct and protect these benefits by delineating levels of appropriated and troop-financed funding responsibilities to promoting American jobs and products to setting boundaries on products and programs that can be offered.

Our growing affinity organization, known as The Coalition to Save Our Military Shopping Benefits, represents over 2 million service members, veterans, and their families; and is comprised of some of the largest, oldest, and most trusted military and veterans' service organizations in the country, as well as those representing our newest veterans and military family members.

We all share a common purpose and commitment to work together to strengthen the foundation of this program so that it can endure any challenge. This partnership represents the best that America offers and is a shining example of what can be accomplished when Government and American business get together for a common purpose.

These operations continue to economize and evolve. They have to. In addition to benefits, they are businesses—that's what businesses do, strive to increase sales and reduce costs. And, that's what they've been doing for years.

Before we talk about concepts such as budget neutrality, costs of goods sold, return on investment and other budget and business terms:

Let's pause for a moment and think what this system is really all about.

Let's pause for a moment and look at the faces behind the bases.

Today, as we assemble here, across the globe, millions of America's military are going about their day, getting their children off to school, balancing their household budgets, thinking about their loved ones deployed, going to work and doing what every American family does. They are most likely going to visit one of the thousands of exchange, commissary and MWR facilities on base to drop their kids off at the child care center, go the gym, take advantage of a multitude of off duty respites.

There's a military spouse at the commissary or exchange, partner deployed, gathering her coupons, loading children into the shopping cart in the parking lot, seeing other spouses, being greeted by a friendly face, and being greeted by a commissary or exchange employee that may be one of them, but certainly is someone that understands the challenges of military life. They feel good about military life.

They enter a new gleaming store. They know this is "their" store. They feel good about military life.

As they go down the aisles of the exchange or commissary they are uplifted by the vast array of recognizable American products. They feel good about military life.

They see affordable, healthy options. They feel good about military life.

They glance down at her kids and they feel good about military life. They see another military spouse working in the store and another person's child bags her groceries. They feel good about military life.

They run into a neighbor whose partner is deployed and get to talk about their shared experiences running a household on their own. They feel good about military life.

They run into a Veteran shopping with his family and they feel good about military life.

They go to the cash register and get a great deal. They have increased financial security. They feel good about military life.

They use their savings to perhaps buy something special for her children. They feel good about military life. Maybe they go over to the new youth center afterwards. They feel good about military life.

They know America is thankful for their sacrifice and service. They feel good about military life.

They may be a beneficiary or familiar with the vast number of commissary and resale supported benevolent causes such as Snowball Express, USO, the National Family Association, scholarships for military children, and other programs. They feel good about military life.

They know that when they go to the next base that they will have the same experience. It's a stable and predictable experience that they have from base to base. It's an anchor in an otherwise very difficult environment. It gives them peace of mind and strength to deal with all of the travails associated with their partner's service. In other words, it makes them feel good about military life.

And today, as we sit here, we should feel good. We should feel good that we have given them and millions of others these benefits. We should feel good that they shop at the exchange and the commissary, facilities that they built with their contributions. And, we should pause and remember why we are here. We should pause and appreciate what they have earned. We should pause and appreciate what our responsibility is to protect and preserve their vital benefit. And we should pause and appreciate what is at stake if we do the wrong thing.

We believe the commissary program delivers tremendous bang for the buck. Let me offer some perspective—some proportionality. Last year, this subcommittee adopted major reforms to retirement under the belief that it was not fair only to allow 16 percent of the force to be able to secure their retirement. This year, you have announced that you are looking at health care reform. Together, these programs consume over \$100 billion a year. The commissary program consumes just over \$1 billion a year in direct appropriations—1 percent of retirement and health care and less than one-half a percent of total compensation spending by DoD. So, only 16 percent can benefit from the current retirement system and 80 percent of health care expenditures are spent in the golden years. But, the commissary benefit is available and used by all military, by all ranks, guard and reserve, active duty and retired, immediately and throughout their career, and by surviving families—and it is used a lot. And, it's a benefit that kicks in when it is most needed, by troops with families in junior grades and by fixed income annuitants.

Ever since the DoD began proposing reductions to the commissary budget, this committee has engaged productively to ensure that any changes were carefully deliberated. We weren't afraid of analysis. We were afraid of no analysis.

The Committee affirmed its belief in the value of the benefit and its commitment to preserving it. You got that right.

The Committee said that a careful plan and strategy should precede any budget reductions that would diminish patron savings. You got that right.

The measured approach fostered by you and the other committee members called for a comprehensive study of the commissary and exchange program to ensure that it was modern, efficient and responsive to existing and evolving patron preferences. You got that right.

The Committee stated that any changes should not diminish the level of savings provided to commissary and exchange beneficiaries. You got that right.

The Committee took no reductions to the commissary or exchange appropriations pending a careful review. You got that right.

It's the next iteration of this evolution—taking concepts to practice—where we face the most peril.

Mr. Chairman and members of the Committee—keep in mind that as big a contribution that these programs make and the long and proud tradition of service, they are perhaps the most fragile and vulnerable of all benefits. This is because of the way they are funded. They are at ground zero of the fast spending, outlay rich operation and maintenance funds that are most vulnerable to reductions. The commissary appropriation is not an entitlement in the sense that health care, retirement, pay and other benefits are. While there are rules for administering the programs in Title 10, there is no floor on funding and while the law says that goods must be sold at cost, DoD can de-fund the programs at any time. Also vulnerable are nonappropriated funds. This committee has a long-standing tradition of safeguarding the nonappropriated fund trust and worked to establish boundaries over the use of these funds. These funds are generated from the earnings of MWR and exchange programs. Essentially, military folks tax themselves to provide funds for the modernization of their own facilities. As pressure builds on the budget, there is a great temptation to use these funds for purposes other than why they were generated to backfill shortfalls in other base operations areas. Any inappropriate diversion of these funds is a disservice to the troops and, in turn, exerts great pressure on exchanges to provide dividends and reduce their capital expenditures.

The DoD is working on the report requested in the 2016 NDAA conference report. We hope and suspect that as decision-makers in DoD peel this onion back, they will realize what we already know---this system works. It is strong yet fragile. That there is a carefully constructed commerce ecosystem on base that is susceptible to tampering and that pulling the thread too hard and too fast could unravel what has been built. Any reductions to funding need to be carefully measured.

We know the system has to change. And, we view the action by the Armed Services Committees as an opportunity to allow the system to evolve--be more efficient, more relevant. We hope that the system can evolve methodically and responsibly.

We need to break down legislative, bureaucratic, cultural, and regulatory barriers to patron convenience and choice.

We need to continue to work to make the shopping experience relevant. Offer what off base retailers already recognize: today's military is more tech savvy, better paid, more educated, and more sophisticated and discerning.

We need to break down the barriers to product assortment restrictions between exchanges and commissaries in manner that does not disadvantage either entity to allow a broader array of products and services to be offered in a one-stop shopping facility. That's what folks outside the base are getting used to and that's what we need to offer.

We need to unchain the system from archaic restrictions on personnel and management and give resale leaders and managers the tools they need to be more agile and market responsive.

We need to streamline the "go to market" capability to ensure that the latest products get to patrons fast.

We need to improve technology including back of the house IT cooperation among resale programs and leveraging the system's strengths to enhance the internet shopping experience. But any drift to outright consolidation needs to be carefully calibrated. Each resale program has its relationships with its respective Service. These relationships are real. They work to mobilize the systems and ramp them up in time of wartime mobilization. They are brands that the troops and their families identify with. And, the DoD's Defense Business Optimization Board is a step in the right direction in

leveraging the strengths of the systems and bringing them together where it makes common business sense and yields positive results.

We need to leverage each resale entities' relative strengths, go the highest denominator and harness and bring back of the house systems together to economize but, even more importantly, exponentially modernize archaic financial, technology, human resources, and other systems that drag us down and keep use from propelling forward.

Yes, there is consensus in Congress on commissaries. The consensus is to preserve the benefit, not destroy it.

This committee has consistently affirmed its support for the benefit, fully restored funding cuts, and has been unyielding in its call for no diminishment of savings levels for patrons.

And the Ranking member of the full Senate Appropriations Committee, Senator Mikulski, said that the proposals to reduce commissary programs were wrong. She said: *"The president is wrong," she said. "[Defense Secretary] Ash Carter is wrong on this. These are false savings."*...right before the full Appropriations Committee voted to restore commissary cuts proposed in the 2016 budget request.

Her support for the benefit was echoed by the House Appropriations Committee, which has steadfastly and continuously affirmed its support for the benefit and for two years running rejected any funding cuts.

When moving directly to a privatization pilot was introduced by the Armed Services Committee into the Senate, it was flatly rejected with over 33 co-sponsors and a unanimous vote.

In 2015, months before it called for privatization and elimination of the commissary appropriations, the SASC said:

“Commissaries have a major positive impact on the quality of life of all service members--active, reserve, and retired--and their families. Commissaries, on average, afford savings of more than 30 percent on items purchased. Additionally, commissary patrons frequently use base exchanges when they come on post to shop at the commissary. Increased usage of the base exchanges results in additional dividends that are returned to the military community for morale, welfare, and recreation activities. The cumulative effect of all of these benefits from commissary patronage is particularly important to junior enlisted service members”.

“The committee is concerned that consequences of the Department of Defense proposal to increase costs to patrons of the commissary benefit in order to reduce appropriated fund support for the Defense Commissary Agency have not been fully evaluated, and that other business models that may not have the same detrimental impact were not considered.”

The fiscal year 2016 NDAA asked DoD to examine several alternatives and concepts. We have carefully assessed these and respectfully offer our views:

- ***Establishment of common business practices to exploit synergies between commissaries and exchanges and to optimize operations of the resale system and benefits provided by commissaries and exchanges—***
We agree.
- ***Privatization in whole or in part—***We disagree and our rationale is explained in detail later in this testimony
- ***Engagement of major commercial grocery retailers or other private sector entities to determine their willingness to provide patrons with discount savings on grocery products and certain household goods—***
ALA companies already do this every day with our resale partners.
- ***Closure of commissaries in locations in close proximity to other commissaries or in locations where commercial alternatives, through***

major grocery retailers, may be available. We disagree. Commissaries are already crowded. Closing stores in the same area exacerbates this crowding. It also requires people to travel further to access their benefit and would only yield marginal savings. Further, any commercial alternatives do not offer commissary pricing and run contrary to the DoD's and Congress's stated position of not wanting to diminish the savings levels for patrons. DeCA already has closed over 180 of the 420 stores it had when it was created in 1991 with over ten more closures on the way.

- *An analysis or different pricing constructs to improve or enhance the delivery of commissary and exchange benefits*—We are concerned that this is a Trojan horse that will open the door to price increases and reduced appropriations. We are willing to work with the pilot programs to examine price variations but as it stands now, we have great difficulty in reconciling price flexibility with no reduced benefit.
- *Description of any of these modifications on MWR programs*; --Agree
- *Maintain baseline of patron savings*--Agree

We haven't seen the President's budget for 2017 but we hope that DoD will remove the specter that has been hanging over this system for three years—drastic cuts programmed into the budget that have had to be rejected and restored with great effort by this committee and other committees of Congress.

Of course, we haven't yet seen the plan for budget neutrality set forth in the Fiscal Year 2016 NDAA and therefore can't formally comment on what that plan may entail.

In recent months, we have detected a notable shift in tone from the Pentagon regarding the resale system. It appears a more measured and deliberative approach is settling in that puts the achievement of efficiencies ahead of cuts. It appears to be recognition by the Secretary of Defense and his principals including the Deputy Chief Management Officer of the tremendous value of these benefits, the fragility of the resale

commerce ecosystem and the need to be careful not to throw the baby out with the bathwater when driving to reforms.

DoD's stated intent and publicly released documents just a few weeks ago said: The intent of Defense Resale Optimization is not to:

- Consolidate the commissary and the exchange systems as recommended by the Military Compensation and Retirement Modernization Commission;
- Reduce Defense resale benefits to meet artificial budget goals; or
- Reduce the flow of MWR funds derived from the resale system.

We do know this -- absent any real economies in operations identified by DoD, that the only option is to change product availability or increase prices to patrons. This will have a direct impact on the quality of life of patrons and will also greatly diminish the capability of exchanges to generate needed funds for MWR programs.

Yes, there are reports that suggest major reforms including the Boston Consulting Group (BCG) report and the Military Compensation and Retirement Modernization (MCRMC) report. But both these reports say that the benefit is worth saving. And then we have reports by ALA, Rand and by the Business Executives for National Security (BENS) that say that the system is working well and needs to be preserved. BENS said that the benefit shows a positive return and has always equated to less than 1 percent of the military compensation benefit. And, BENS said that from 1992 to 2014, the commissary cost has held steady in constant dollars. And, BENS points out that 64 percent of commissary jobs are held by persons connected to a military service member. DoD itself commissioned a RAND report that had some revealing findings. RAND said that 80 percent of enlisted and 70 percent of officers ranked commissaries as "high" or "the highest" of nonpay benefits. RAND cites an increase in the price of commissary goods would likely reduce both recruitment and retention. RAND says that an increase in commissary prices will result in an increase in cost of living allowances. And, RAND points to commissaries maximizing SNAP and WIC payments to the troops and that these

coupon redemptions have increased 300 percent. And, the BCG report stated that a 5 percent increase in commissary prices would result in a 30 percent drop in sales, sending shudders throughout the entire military resale and MWR ecosystem. While DoD contemplates the construct of a pilot to test raising prices the reports above may give you the answer to the test.

Regarding the BCG report: There is a lot of valuable data contained in the report. The assumptions and data need to be carefully dissected and analyzed prior to buying into their recommendations and the implementation needs to be carefully deliberated by DoD prior to proceeding. Their recommendations on shared support service integration, expanding commissary hours, and providing a more relevant shopping experience track with our views. Some of the assumptions on cost savings from supply chain and cost of goods efficiencies do not track with our data. Their projections on pricing flexibility, cost of goods reductions and other efficiencies are highly questionable and there was a noticeable lack of analysis to support these findings.

Their suggestions on local sourcing need to take into consideration that the troops want American products, made by American workers and companies paying American taxes. Many of the changes involve drastic shifts in the DeCA culture, which will take time. We are formulating our views on specific aspects of this report using our expertise in the commercial and military marketplace. We simply must see the plan for implementing these practices and the hard and difficult translation of their suppositions into practice in a dynamic military marketplace.

Exchange systems operate under fewer restrictions using a nonappropriated fund business model and have different pricing processes. Their prices are set using data provided by IRI and Nielsen and set target margins. Commissaries use a cost-plus 5 percent pricing process. BCG says that this process causes DeCA to incur a net loss on each transaction. True, but this is because it is a benefit that is intended to provide discounted products. If you take this view, then DoD loses 100 percent on each health

care transaction and 100 percent on each pay transaction and 100 percent on each housing support transaction.

The Department will present pilots to the Congress. These pilots may ask for pricing flexibility to allow commissaries to operate more like commercial grocers. These pilots may depart from the cost plus five model but under the guidelines cannot diminish the overall savings to the patron.

The pilots may seek to increase margins by introducing more private label products and negotiating lower cost of goods sold. Two issues here: 1) Under price warranties, manufacturers already have to give commissaries the best price, and 2) If the purpose of private label is to provide deep discounted non-name brand products, you defeat the purpose by raising the prices to increase margin to offset appropriated fund expenditures. We will be very interested in how these pilots are structured because right now it's tough to see how you reconcile margin increases while maintaining overall patron savings. DoD may propose increasing prices on some products and decreasing prices on others or raise and lower prices depending on geographic region. It's tough to see how this will generate funding without diminishing patron savings and we are going to very interested in how geographic pricing variations do not diminish savings for military personnel who are all paid the same wherever they serve.

And, in order to manage all of this, there will be a big learning curve for DeCA category managers who must fundamentally change the way they do business and conduct product negotiations.

There already are templates for pilots that exist or can be resurrected to economize operations, especially at smaller bases. A hybrid operation was piloted at Carswell Air Force Base but the rules and restrictions did not allow it to meet its full potential. Here, commissary items were sold at cost and exchange items were sold at a markup. The flaw was that the amount of appropriations that could be transferred to compensate for any losses to the NAFI was restricted to 25 percent of the funds that were

authorized for that location before the pilot. Fix that and you have a running start at a hybrid solution.

Within the Navy, there are several hybrid operations running. These Nexmarts mix NAF and appropriations to provide services at selected locations where it is uneconomical to operate exchanges and commissaries separately. This model can be extrapolated and exploited to reduce costs without reducing benefits.

And, in any pilots, cooperative efforts and shared services, there needs to be the ability to share in the savings that take place so that you are not punishing success. We need to ensure that any savings that are generated through any contracts or agreements are apportioned based on the level of participation and contribution. The DoD's Resale Optimization Board provides the vehicle and conduit to realize this principle.

Another BCG proposal is to bring vendor stocking in house. Many of our members currently provide these services. We look forward to working with DeCA to see how this transition would work and whether indeed it yields savings to DeCA if more of this function is brought in house.

Another area identified by BCG is to NAF the process of acquisition so that DeCA no longer uses the Federal Acquisition Regulations. There's a reason these regulations are in place for appropriated fund purchases. It's to protect the interests of the Government. We are going to be very interested in seeing how deviation from the FAR will reconcile protecting Government interests with flexibility. Nevertheless, we support more flexible and streamlined acquisition processes.

While the devil is in the details, we see merit in several other BCG recommendations including:

- Rationalizing capital expenditures among the exchanges and commissaries and would advocate more efficient and streamlined commissary construction procedures.
- Providing for broader participation of military affiliated personnel including Federal civilians and veterans serving in the executive branch.
- Broadening flexibility to mix appropriations and NAF to provide for acquisition synergies including authorizing the use of both appropriated and nonappropriated funds on contracts or agreements for the acquisition of common business systems for the Defense resale system or to exploit acquisition synergies in obtaining logistical services, supplies, and resale goods and services.
- Authorizing DoD to enter into agreements and contracts for products and services that are shared by commissaries and exchanges and for the acquisition of supplies, resale goods, and services on behalf of both commissaries and exchanges.
- Authorizing reimbursement of NAF with appropriations for the portion of the cost of the contract or agreement entered into by the NAFI that is attributable to the commissary system.
- Authorizing the commissary system to accept reimbursement from a NAFI for the portion of the cost of a contract or agreement entered by the commissaries that are attributable to the NAFI.

With regard to pricing pilots, a major factor to consider is patron confusion. Military folks move from base to base. Will they see one model in one commissary and a different model in another and how can we expect them to understand what is going on? We're not sure what is to be gained by increasing prices in one category and dropping them in another but we will keep an open mind.

BCG says that these pricing experiments are needed to gauge patron acceptance of pricing variations. I can save them some time right now: If you raise prices on a

product, people buy less of it. If you raise prices on one category and lower them on another, you generally come out the same. If you regionalize prices, it seems you have to regionalize pay if you want to keep the benefit equitable.

And, you won't be surprised that we are dubious about price variations. It's usually code for price increases. We are all for efficiencies but still have difficulty seeing how DoD could ever come close to achieving elimination all appropriated support for commissaries and exchanges. In fact, CBO sees the same thing. In August of 2011, when the Senate Veterans Affairs Committee was considering resale reforms and wholesale repeal of Title 10 protections needed to pay for the Camp Lejeune water contamination damage, it asked CBO to score the resale reforms needed. CBO said that consolidation and efficiencies would only account for 20 percent of the savings to the \$1.7 billion appropriation for commissaries and exchanges. They said that the rest of the savings would have to come from price increases to the troops.

ALA is an organization of businessmen and women. We know that businesses need to evolve to changing market conditions and that DoD needs to squeeze every dollar out of appropriated funded operating costs as possible. We are prepared to roll up our sleeves and work with DoD to do just that.

The pilot authority set forth in the NDAA allows waivers of existing law. We are very concerned that the laws that DoD is considering waiving are those that effect pricing. In the event that more private labels are introduced, would these products be sold at cost or at a mark-up to provide funds to pay for commissary operations? If so, you are defeating the purpose of private label if their introduction merely results in increased prices for non-name brand products.

Any savings shared by commissaries and exchanges should be based on their participation. These savings should be shared by the defense commissary system and the exchange system through contracts or agreements that reflect the participation in the development and implementation of such practices.

We can make other changes now that would greatly improve the quality of products and services offered our military folks while economizing on use of appropriations and generating revenue:

Let's collectively get together and get the MilStar card into the commissaries. Significant annual value of \$110 million to \$199 million can be created for the military community with limited one-time costs. Most importantly, military families will realize additional savings and convenience as well as enjoy improved support of Morale, Welfare and Recreation programs. A seamless approach to consumer credit at exchanges and commissaries strengthens customer engagement and represents a logical and necessary progression in military resale/quality-of-life cooperative efforts.

Let's collectively get together and bring the Veteran On-line Service Benefit to reality. Here's program espoused by the exchanges that provides benefits for veterans, will increase earnings to MWR programs and provides a benefit for many involuntarily separated veterans with limited access to benefits. We should find a way to do this that VA and DoD can agree on and get on with it.

Let's work to coordinate and reduce duplicative food offerings among MWR, exchanges and commissaries and examine the use of the basic allowance for subsistence and troop meal cards for use in exchange food outlets and coordinate all food offerings, including commissaries, in support of DoD's Healthy Base Initiative.

Let's collectively get together and finish what was started when the Committee authorized the exchanges to access the Federal Financial Bank for reduced finance charges. Congress—this Committee and House Financial Services, supported it. It's time to bring this into practice.

Let's give exchanges the ability to offer the sale of fuel to government vehicles to get around higher DLA fuel prices.

Before any employees are considered to be converted to NAF, let's expand the existing statutory authority for portability of benefits to provide parallel protections. Let's extend the MWR Unified Funding and Management and Utilization Support and Accountability authorities to commissaries and exchanges. And, let's look at exempting NAF contracts from the Service Contract Act.

Let's not impose government-only labor cost hikes on exchanges that place them at an unfair competitive advantage with off-base entities and raise prices to military patrons.

Exchanges provide dividends to MWR programs. MWR programs need to economize and reduce the pressure on the exchanges to generate dividends. Let's look at the structure and overhead of these programs to ensure that there is no waste, that they cooperate to reduce common support service costs, reduce appropriations and dividend demands and take out some of the hundreds of millions in overhead costs that are associated with the management of these programs. There are admirable efforts already underway in DoD in this regard and they need to be encouraged and exploited.

We are also concerned DoD might suggest using the pilot legislative waiver authority to implement changes not at individual stores but system wide. We don't believe that this blanket waiver is in keeping with the spirit and intent of the provisions set forth in the 2016 NDAA.

Let's talk about budget neutrality. The conferees on the NDAA said that the DoD needs to come up with a plan to have the system be budget neutral by 2018. Set aside for a moment that this is a requirement that has been placed on no other program in the Department of Defense in the history of our Nation. It is a stretch goal that no other program is even close to being asked to make. I remember when Colin Powell, as JCS Chairman, was presented with reforms to this system during his tenure. He said: "If it ain't broke, don't fix it." And, we all need to be careful to not fix something that ain't broken.

We submit that by any definition, the military's commissaries and exchanges have met the requirements set forth in the Fiscal Year 2016 National Defense Authorization Act to be budget neutral.

Under the definition of no increase or decrease from year to year, these programs are already budget neutral and have not had a net increase in appropriations levels in non-inflation dollars for the past 25 years, and in fact, these appropriations have decreased. This does not include funding required to support direct mission requirements needed to support overseas deployments including Afghanistan and Iraq. No other program in DoD can make the claim that costs have actually dropped over the years.

Under the definition of no net outflow from Treasury these programs are already budget neutral in that they generate more back to the DoD and the Treasury than they consume.

Currently the commissary system relies on appropriated funds to pay its operating costs. In fiscal year 2015, the commissary system has received appropriations of approximately \$1.3 billion to pay for the salaries of employees, the transportation of its inventory, and other costs associated with operating and maintaining approximately 250 stores. The commissary's inventory is financed on a revolving basis, using the cash generated from sales of that inventory. In inflation-adjusted dollars, since the Defense Commissary Agency was established in 1991, this support is \$653 million.

The three exchange systems are less reliant on appropriations. Although certain expenses of the exchanges are paid for through appropriations—including the transportation of certain items and the salaries of military personnel employed by the exchanges—the majority of the exchanges' costs are funded from sales revenues generated by the exchanges. Based on information from DoD, CBO estimates that appropriations provided to DoD cover approximately \$200 million of exchange-related costs annually. In inflation-adjusted dollars, since 1991, this annual figure has dropped to under \$100 million.

Total inflation adjusted appropriations is approximately \$750 million to support both exchange and commissary programs, down from \$1.2 billion in 1991.

These costs have been reduced by increased efficiencies in both the exchanges and commissaries, largely attributed to five rounds of base closures that have reduced the number of bases where these stores operate by 40 percent since 1991. Efficiencies generated by the exchanges and commissaries have further reduced Treasury outlays.

Further, these programs continue to generate funding back to the Government and directly offset taxpayer obligations including nearly \$700 million each year in funding for physical assets that accrue to the balance sheet of the Federal Government and direct funding to military installations to support community morale programs.

Even using the non-traditional and stricter definition of “budget neutral”, these programs are budget neutral because they generate more back to the government than they spend. In direct Treasury outflows, and when direct cash contributions by the system to the Government are measured against the appropriations spent, the system yields \$373 million per year in proceeds in the form of reduced outlays to the Government. Elements of this offset include Federal tax paid, reduced cost of living allowance requirements and physical asset and contributions to military community morale programs generated by the exchanges.

Mr. Chairman—No other Defense program can come close to making these budgetary and savings claims. It’s a public private partnership efficiency model that should be replicated in defense, not decimated.

On introduction of private label, our concern is that the complex actions and competitiveness of the private label business will require DeCA to invest significant resources (appropriated dollars) without a test to validate its cost/benefit. There doesn’t seem to be a test to validate DeCA’s assumptions. Furthermore, DeCA currently has a comprehensive Value Brand program that affords the military patrons opportunities to purchase alternative brand name products, especially those who use SNAP. Is there

an assurance from DeCA that any private label initiative will not result in higher prices to its patrons than the value brand program that now exists?

In addition, branded manufacturers provide a significant amount of support to DeCA either directly or through their representatives. Examples of this type of support would include: promotional trade spending, retail store support to include schematic sets, distributor management, and promotional signage, shelf stocking, and working with stores to keep CAO data accurate. It doesn't appear that DeCA has considered the impact of reduction in support from its branded suppliers if it pursues private label.

It is industry's recommendation that pursuing a comprehensive private label program hasn't been properly reviewed to determine its full impact on the military patron as well as the appropriated dollars. A significant amount of money that would be necessary to standup and manage such a program, which the national brands currently include in their cost of goods, should be evaluated.

- Closely define the parameters for any test of variable pricing to ensure a proper evaluation of the model is reviewed and accepted before expansion. We would suggest no more than one or two product categories are included in a test for evaluation. Patron savings levels must exceed current patron savings levels in the test categories.
- Because of the importance of the value brands to the young military family, DeCA should be required to evaluate current levels of patron savings from value brands by category. They should test no more than 1 or 2 categories with private label and must achieve better patron savings level than the value brands currently deliver in those categories.
- DeCA should consider best source pricing by category for its private brands that will include current value brand suppliers.
- Any incremental cost of developing and implementing a private label program, as well as a variable price program, should be included in the patron savings calculation.

Mr. Chairman, each day, tens of thousands of dedicated nonappropriated funded employees and nearly 16,000 commissary employees report for duty. These employees care greatly about their mission, providing a wide range of vital programs and products in the far corners of the globe and in some pretty dangerous areas. They deserve our consideration and respect. As far as commissary employees are concerned: with all the recent talk of changing their employment status to NAF, privatizing the commissaries, and eliminating the appropriated support, I'm reminded of the expression: "*The beatings will continue until morale improves.*" This is a group of people that have performed exceptionally well—leading the DoD in accountability of resources, delivering a great benefit day in and day out, leading the Department in energy conservation, veteran hiring, small business contracting, equal opportunity, and so many other areas. They deserve our support and appreciation and not implied or direct criticism of their dedication and exceptional effort.

This past year the resale system has been buffeted with continuing efforts to restrict product availability impose restrictions on operations by many well-meaning constituencies. Whether it's tobacco, alcohol, energy supplements, sugar or other products, we need to keep in mind that the troops are not guinea pigs in a laboratory. Besides warriors, they are first citizens—and they are charged with defending freedom. But reformers including individual members of Congress and advocacy groups make continual runs at placing restrictions on what products they can buy on base. They do this because military bases are Federal enclaves and they can do things there that they can't in adjacent municipalities. The proposition is simple. If it's a legal product off base, it should be legal on base. This Committee has a long history of defending these rights and privileges and has served as the gatekeeper in Congress to product category authorizations that recognize the principle of open access to legal products. We hope that you will continue to exercise this oversight and advocacy role on behalf of the servicemembers and their families.

We carefully follow the overall debate on Defense spending and the concerns raised that compensation is consuming an increasing part of the Defense budget and that

these expenditures are detracting from direct combat readiness expenditures. While we think that the answer is not to reduce compensation but to increase defense spending, we get that all aspects of DoD need to be accountable and efficient, including commissaries and exchanges. But, keep in mind that commissaries and the availability of healthy products directly contribute to readiness by keeping good people in the service and providing for a health force. A November 2015 report by the Surgeon General of the Army found that fully one third of the troops report that healthy food is too expensive. To quote from the report: “These obese service members in the brigade in Afghanistan were 40 percent more likely to experience injury than those with a healthy weight, and slower runners were 49 percent more likely to be injured.”

As directed in the Senate version of the 2016 NDAA, the Comptroller General is conducting a review of privatization of commissaries and exchanges and this report was to be provided to Congress at the end of this month. ALA and several of our member companies have met with the GAO and expressed our concerns with the outright privatization proposal.

We agree with outsourcing where it makes sense but not outright privatization. Major commissary functions already are outsourced. Distribution for commissaries was outsourced in 1996 and nearly \$500 million was returned to the DoD’s stock funds when this transition took place. Several in-store functions including bakeries and delis are outsourced as is shelf stocking, produce distribution, and myriad other functions. Exchanges have a special status as instrumentalities of the United States government whereby they already adopt commercial business practices while enjoying the immunities of being a Government entity.

We believe that the current mix of outsourced functions and government-operated functions should be maintained. It affords the DoD the immunities and protections of a Government entity while providing the advantages of outsourced functions where they make sense.

- We need to consider the impact on the workforce from privatization.

- What is to come of the myriad social programs that commissaries and exchanges support such as small business mandates, Javits Wagner O'Day benefits, the Ability One program and equal opportunity programs?
- Outright privatization of commissaries has been considered by the Department of Defense and actually tested on one occasion. The test didn't work.
- The Military Compensation and Retirement Modernization Commission examined privatization but did not to recommend it.
- It would be difficult to find a private operator to deliver the same level of benefit, especially as the DoD has also been directed to reduce appropriations for commissaries to zero by 2018.
- If prices are increased, what private operator would come on base and only serve the limited on-base market where no patrons choose to come to parity priced grocery store on base.
- A private operator would probably cherry pick the high volume stores and set the small and remote stores adrift.
- When the DoD privatized lodging in the Army, temporary lodging rates skyrocketed and facilities were not capitalized as promised.
- Contractors would seek Government guarantees as a backstop against base closures and force structure reductions. These guarantees would "Score" against the DoD budget.
- What would happen to the billions of dollars of facilities that patrons themselves invested in? Would they be compensation for these investments? If privatization is even being considered, shouldn't there be a moratorium on charging patrons a capitalization surcharge until the issue is resolved?
- Privatization will result in higher prices on groceries for military families. DeCA and the exchanges already receive best pricing from most manufacturers, so regardless of which private contractor operates the

commissaries, the price they receive from manufacturers will not be lower than what commissaries and exchanges currently receive.

- Under current law, private entities that operate on base as concessionaires to military exchanges are required to collect sales tax. That means military families would be required to pay sales taxes on groceries purchased in a privately operated commissary.
- Many commissaries and exchanges are located in areas where other shopping options do not exist will never generate enough sales revenue to offset their cost of operation. There is great concern the contractor will cherry-pick profitable stores while abandoning stores that do not generate a profit leaving military families with no source of meeting their basic needs.
- The cost of operating a privatized commissary or exchange will be higher in that some current roles and functions in commissaries and exchanges are provided by private industry. Distribution, promotions, and shelf stocking are already performed by private entities and helps to reduce the cost of operations. A private entity will be required to pay for those functions, thus increasing the cost of operations.

Mr. Chairman, this concludes my remarks and I would be delighted to answer any questions you may have.