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VIEWS ON COMMISSARY REFORM

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BEFORE THE

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COMMITTEE ON ARMED SERVICES
HOUSE OF REPRESENTATIVES

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VIEWS ON COMMISSARY REFORM

HOUSE OF REPRESENTATIVES,
COMMITTEE ON ARMED SERVICES,
SUBCOMMITTEE ON MILITARY PERSONNEL,
Washington, DC, Wednesday, January 13, 2016.

The subcommittee met, pursuant to call, at 10:30 a.m., in room 2118, Rayburn House Office Building, Hon. Joseph J. Heck (chairman of the subcommittee) presiding.

OPENING STATEMENT OF HON. JOSEPH J. HECK, A REPRESENTATIVE FROM NEVADA, CHAIRMAN, SUBCOMMITTEE ON MILITARY PERSONNEL

Dr. HECK. Well, good morning. I want to welcome everyone today to today's Military Personnel Subcommittee's hearing on commissary reform. We are here today to hear from military service organizations and the grocery retail industry on the value of the commissary system to beneficiaries and the effects of any possible changes to the commissary's business model. As we are all well aware, commissary benefits are a valued part of our current and retired service member's compensation package and contribute to their and their family's overall quality of life.

The Military Personnel Subcommittee is taking every opportunity to thoroughly review and discuss the way forward on any commissary reform, and is committed to retaining the commissary benefit while improving the business practices of the commissary system and at the same time reducing its dependence on appropriated funds.

Our purpose today is to gain an understanding from the panel on their views of the possible effects to the beneficiaries or to the business practices of our industry partners of any changes to the commissary system business model.

Before I introduce my panel, I would like to offer Congresswoman Davis an opportunity to make any opening remarks.

[The prepared statement of Dr. Heck can be found in the Appendix on page 27.]

STATEMENT OF HON. SUSAN A. DAVIS, A REPRESENTATIVE FROM CALIFORNIA, RANKING MEMBER, SUBCOMMITTEE ON MILITARY PERSONNEL

Mrs. DAVIS. Thank you very much, Mr. Chairman. And thank you to all of our witnesses. Good to see all of you here today. Our panel represents beneficiaries as well as retail industry partners that work with the commissary system.

I think we can all agree that what is paramount in this discussion is that the commissary benefit must be maintained. How that

happens, though, and what the system will look like is what we are here to discuss. Change is never easy, we know, but in today's fiscal environment, it is required. This committee certainly has met several times since the release of the Boston Consulting Group [BCG] report, and we have heard from the BCG, as well as the Department of Defense [DOD], on ways to sustain the commissary benefit even when we know and we hear that many feel that the commissary system is just not sustainable as it is currently today.

I was pleased to hear from DOD leadership that they concur with the report. Regardless of how much reform is done to create a more efficient business model, keeping the savings that are realized today for patrons is critical.

As we wait to see what the Department will submit to Congress for this year's NDAA [National Defense Authorization Act], I would encourage all of us, all of you to work with the DOD and help us reform a system that will endure into the future.

I look forward to hearing from our witnesses as we work to responsibly and efficiently protect the commissary benefit for our service members and families.

Thank you, Mr. Chairman.

Dr. HECK. Thank you, Mrs. Davis.

I now ask unanimous consent that the following testimony be entered into the record from the American Federation of Government Employees. Without objection, so ordered.

[The information referred to can be found in the Appendix on page 109.]

Dr. HECK. I also want to let our panel know that votes are scheduled some time between 11:15 and 11:30. We will push to 11:30 until the clock actually runs to zero on the vote. My goal is to get the hearing completed so we don't have to hold you here while we go vote.

We are joined again today by an outstanding panel. We will give each witness the opportunity to make opening comments and each member an opportunity to question the witnesses. I respectfully ask the witnesses to summarize to the greatest extent possible the high points of their written testimony in no more than 5 minutes. Your complete written statements will be entered into the hearing record. As a reminder, the lights in front of you will turn yellow when you have one minute remaining and red when your time has concluded.

We are joined today by Mr. Patrick Nixon, President of the American Logistics Association; Mr. Tom Gordy, President of the Armed Forces Marketing Council; Ms. Eileen Huck, Government Relations Deputy Director for the National Military Family Association; and Ms. Brooke Goldberg, Deputy Director for Government Relations, Military Officers Association of America.

With that, Mr. Nixon, you are recognized for 5 minutes.

STATEMENT OF PATRICK B. NIXON, PRESIDENT, AMERICAN LOGISTICS ASSOCIATION

Mr. NIXON. Thank you, Mr. Chairman, distinguished ranking member, Mrs. Davis, committee members, and staff. It is an honor once again to appear before you representing the member compa-

nies of the American Logistics Association and to provide views on commissary reform.

Mr. Chairman, we are always open to new go-to-market strategies, however, we need to play the cards that we actually have been dealt. Until the new FYDP [Future Years Defense Program] is approved, we are facing a \$1 billion reduction in commissary funding in 2017. The GAO [Government Accountability Office] review on privatization is supposed to be completed February 1st. We don't know what that is going to say. Until DOD submits its report requested by the 2016 NDAA on key topics to include a new twist, budget neutrality, we do not know the way ahead. But Mr. Chairman, with these negative headwinds, it is not a time to put one's head in the sand, and we are not the association of no. We are, in fact, bolstered by positive indicators.

First, Mr. Chairman, you and Chairman Thornberry 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. This committee has affirmed its belief in the value of the resale benefit and its commitment to preserving it. It is the next iteration of this evolution taking concepts to practice where we face the most peril.

Mr. Chairman, on the DOD side, there is a new sheriff in town. Peter Levine as the Deputy Chief Management Officer has presented a more tempered view of the way ahead. He has also stated the strategy needs to drive the budget. We also understand that DOD feels the need to conduct a series of pilots to sort out an alternative universe for military resale. This is where we say, proceed with extreme caution.

Mr. Chairman, I have been in this business for a long time and I have concluded that there are three pillars of influence that must be measured in any strategic discussion moving a resale program forward: patron confidence, supplier confidence, and retailer confidence.

Patron confidence in the current business model is rock solid. In the commissary, it is goods at cost with a surcharge. It is the ultimate company store. The patron invests in the system through the surcharge, they build their own stores. It is a brand name business. Items only make it in the system if they have a demonstrated retail presence in the private sector, they only remain in the system if they have a demonstrated customer preference. Its strength is predictability. In a pilot that proposes to change product pricing, whether by store or region, can you improve on the current level of predictability? If you introduced a private label program that requires a retailer to price, position, and promote a product line with artificial customer preference in order to make a profit, can you improve on the current level of predictability? What are you going to tell the patron? This is their store. This is the model they trust.

Supplier confidence is equally important. Brand name goods at cost create a one-of-a-kind business environment. It is the ultimate supply and demand ecology. Patron preference drives what is on the shelf and what stays on the shelf. There are no hidden retail activities like sliding fees, promotional skimming, or advertising pools. Under audited price warranties, the military retailer gets the best pricing from the manufacturer. Manufacturers contribute al-

most \$500 million in costs to offset annually the system through promotional trade spending, stocking, display building, inventory management, and special military events. The introduction of a different pricing model and private label changes the game. What will be the reduction in support from industry if you change the model? What will be the cost to the retailer to develop, position, price, and promote a private label introduction, once again, with artificial patron preference built in? You will be removing proven name brand value items to position private label items to make a profit. What will be the impact on supplier confidence as these pilots proceed?

Finally, there is retailer confidence. First, the exchanges are probably saying, why am I here in this discussion? This is a commissary issue. The fact is the carefully constructed economic ecology and the military resale system is forever interlocked. During the last government shutdown when commissaries were closed, exchanges dropped sales 30 percent. Exchanges are extremely interested in proposed commissary pilots. What if they fail? What will be the impact of patron confidence on their traffic and sales?

On the commissary side, this is uncharted territory. They have done an exceptional job at administering the cherished military benefit, but becoming a retailer is different. They have weathered a government shutdown, employee furloughs, and now they await a privatization study, a budget neutral discussion, and the outlook of a non-appropriated fund workforce. Reminds me of the saying, the beatings will continue until morale improves.

When it is all said and done, these discussions will be critical for preserving this important benefit or moving forward. I commit the resources and expertise of the American Logistics Association to make this move forward successful.

Thank you for this opportunity to participate, and I look forward to our discussions, Mr. Chairman.

[The prepared statement of Mr. Nixon can be found in the Appendix on page 28.]

Dr. HECK. Thank you, Mr. Nixon.
Mr. Gordy.

**STATEMENT OF THOMAS T. GORDY, PRESIDENT, ARMED
FORCES MARKETING COUNCIL**

Mr. GORDY. Chairman Heck, Ranking Member Davis, and distinguished members of the Personnel Subcommittee, thank you for your commitment to our warriors and their families, who continue to tirelessly serve and sacrifice in defense of our Nation. And thank you for the opportunity to share views on behalf of the Armed Forces Marketing Council regarding efforts to reform the commissary benefit.

As you are aware, to date there are no specific reforms that have been publicly proposed by the DOD since the NDAA was passed and signed into law last month, but from that law, we are very grateful for the committee's work to establish benchmarks for any potential reform efforts, which include ensuring high levels of customer satisfaction, the provision of high-quality products, and the sustainment of discount savings.

As we begin our discussion today, we believe it is helpful to remember that it was Congress who established this benefit as a

non-pay compensation benefit for military personnel. The model that Congress forged is one that is as brilliant as it is simple: offering products at cost plus 6 percent to provide military families a non-pay benefit.

While no specific formal proposals have been offered to the committee over the course of the past 2 years, suggestions have been offered for commissary reform by both the Military Compensation and Retirement Modernization Committee and the Boston Consulting Group that would alter the model. The suggestions call for a more complex operational model through untested and under-analyzed pricing schemes and adjustments to product assortment, which will require growth in both personnel and operational costs.

Since it is highly unlikely that appropriations will be increased to cover these costs, the revenue will have to be generated, and it can only come from one source, and that is the military family.

The suggestions that have been offered are based on assumptions that product and pricing schemes are manageable and would still offer a benefit to military families, but even the suggestions have a caveat that they need to be further analyzed. We agree. And we also believe that full spectrum analysis should be conducted on all efforts that would change DeCA's [Defense Commissary Agency's] fundamental mission and seek to generate revenue from military families.

We also believe that accountability for the commissary benefit should remain with Congress. We hope that if the reform test pilots begin to fail to meet established benchmarks, and if the DOD fails to act in an expeditious manner to protect the benefit, that Congress will step in to do so.

We appreciate the committee's approach that permanent changes to title 10 will be based on concepts that are proven to be beneficial and efficacious to the long-term viability of the commissary benefit. Since commissaries are only one part of the military quality-of-life ecosystem on military bases, which also include the military exchanges and MWR [Moral, Welfare, and Recreation] programs, and that there is an interdependent relationship between these three organizations, we agree with Congress that any effort to reform commissaries should weigh the impacts on exchanges and MWR.

While the budgetary pressures of ongoing deficits and the sequester have forced DOD to make painful cuts to numerous programs, we recognize that resale is not immune to the pursuit of efficiencies. We have always held that efficiencies can be achieved within the commissary system, and should occur as long as they do not result in higher prices and diminished benefits for military families.

We agree with DOD's Deputy Chief Management Officer, Peter Levine, that efficiencies should drive the budget, and are encouraged by this new approach within DOD.

As we consider commissary reform, it is important to remember the words of Lee Scott, the former CEO [chief executive officer] and current board member of Walmart, who said, rule number one of retailing is don't aggravate your customer. Unfortunately, some have learned this truth the hard way. Two examples include Walmart's clean store policy and JC Penny's attempt to offer everyday low prices to its customers, both of which resulted in signifi-

cant sales declines and the firing of senior leaders. They listened to their consultants and even their customer surveys, but the changes ended up aggravating customers, who either purchased less and/or shopped elsewhere. Therefore, we approach reform efforts cautiously due to these recent real world examples which demonstrate how sensitive the retail marketplace is to change.

As BCG discovered, even a 5 percent increase in prices in the commissary would result in 26 percent decrease in traffic. In other words, to generate \$143 million in revenue would cost DeCA \$1.3 billion in lost sales. That should serve as caution to anyone interested in commissary reform that efforts should be fully analyzed and evaluated and carefully implemented. Thus, reform efforts should be a game of inches, proceeding slowly and only implementing concepts that can be easily reversed if negative effects begin to occur.

Chairman Heck, I look forward to your questions in discussing specific suggestions for reform with you and the committee. I yield back.

[The prepared statement of Mr. Gordy can be found in the Appendix on page 62.]

Dr. HECK. Thank you.

Ms. Huck.

**STATEMENT OF EILEEN HUCK, GOVERNMENT RELATIONS
DEPUTY DIRECTOR, NATIONAL MILITARY FAMILY ASSOCIATION**

Ms. HUCK. Chairman Heck, Ranking Member Davis, and members of the subcommittee, thank you for the opportunity to present testimony on the military resale system and its value to military families.

Military families tell us that the commissary is one of their most valued benefits. While we understand and appreciate the need for efficiency and fiscal restraint, we caution against making changes to commissary funding levels or operations that put at risk a benefit many families rely upon.

When discussing the commissary benefit, it is important first to understand what that benefit really is. Our association has argued that the commissary benefit is not just the existence of a brick-and-mortar grocery store on an installation; rather, the benefit is the savings that service members and families see when they shop at the commissary. Those savings are a vital non-pay benefit relied on by many military families, especially junior service members and those families in remote or high-cost locations. Any proposal to alter the commissary operating structure or reduce its funding level must, in our view, also preserve the savings. Those savings are not insignificant.

The Defense Commissary Agency, or DeCA, reports that families who regularly shop at the commissary save 30 percent over civilian grocery stores. We recognize that individual families' level of savings will vary based on their location and shopping habits. However, DeCA's mandate to sell groceries at cost plus 6 percent provides all military families with the assurance that they will be able to put food on the table at a reasonable cost regardless of where they are stationed.

The unique challenges of military life increase the importance of the commissary benefit. Due largely to frequent military-ordered moves, military spouse unemployment rates are far higher than their civilian counterparts. For this reason, many military families must get by on a single income. Many junior families actually qualify for nutrition assistance through the Women, Infants, and Children, or WIC, program. Commissary savings allow those families to stretch their food dollars and help ensure that even the most junior service members can feed their families.

We hear often from military families who tell us how much they value the commissary benefit. When we posted an article on our Web site about recent proposals to cut commissary funding, dozens of military families wrote back to share their experiences with the commissary. One military spouse wrote, "We are a family of six and have been in the military for 17 years. The commissary is something we have relied on at every duty station we have been. We are currently stationed in Alaska and use the commissary and the exchange on a weekly basis. With the prices in Alaska being higher than what we are used to, the comfort of the commissary made it easier to make sure I have all I need to feed my family."

Several recent proposals regarding the commissary include plans to reduce the appropriation and use revenues generated by commissary sales to operate the resale system. We ask you to consider, if such a plan is adopted, what would happen if revenues were to decrease. This concern is not unfounded. Last year the Department commissioned the RAND Corporation to study what would be the effects of increased commissary prices. Not surprisingly, RAND found that if prices increased, fewer military families would choose to shop at the commissary, leading to a reduction in commissary revenue. We fear that faced with lower revenues, DeCA would be forced to reduce operating hours, lay off employees, and ultimately close stores in order to cut operating costs.

We are gratified that the DOD has expressed a commitment to preserving commissary savings in its recent factsheet on the resale system. However, much depends on how DOD defines what it calls the tangible and intangible elements of the benefit, and what metrics it uses to ensure its goals are met.

We ask Congress to require transparency from the Department as it develops plans to optimize the resale system. Military families deserve the assurance that any changes to the military resale system prioritize their well-being.

In closing, we note that maximizing revenue has never been a priority for the commissary, nor should it be. The mission of the commissary is to provide military families with a vital non-pay benefit, the savings they realize by shopping there. In our view, DeCA has fulfilled this essential mission effectively and well. Before making any changes to the commissary's operations, we ask that you first consider the impact on military families, who rely on commissary savings to help ensure they are ready and able to support their service member.

Thank you very much for the opportunity.

[The prepared statement of Ms. Huck can be found in the Appendix on page 84.]

Dr. HECK. Thank you.

Ms. Goldberg.

**STATEMENT OF BROOKE GOLDBERG, DEPUTY DIRECTOR FOR
GOVERNMENT RELATIONS, MILITARY OFFICERS ASSOCIA-
TION OF AMERICA**

Ms. GOLDBERG. Chairman Heck, Ranking Member Davis, and distinguished members of the subcommittee, thank you for holding this hearing on commissary reform.

Your defense of this landmark benefit that has supported military personnel and their families for generations is critical to its continued existence today.

I am pleased to be here to represent more than 390,000 MOAA [Military Officers Association of America] members and as an Air Force spouse of 13 years. I am a regular patron of the commissary and have depended on it during 11 years of my husband's Active service, including 10 deployments for OIF [Operation Iraqi Freedom], and now that he is a reservist.

Repeatedly, advocates come to the Hill to protect this benefit and it has remained protected because of your efforts and support. That support exists because it has intrinsic and real value, and provides a consistent and dependable benefit that would be costly to replace.

Our service members, retirees, wounded warriors, widows, and families know no matter how big or small the town, how far it is from family or familiar surroundings, the commissary will be there. It provides the consistent products, savings, and community they have come to know and rely on from the first day they stepped through the gate.

The amount of money appropriated for the commissary costs taxpayers the equivalent of a 2 percent pay raise to the entire military, but the monetary value to the E-5 with 8 years of service and a family of four is equivalent to a 9 percent pay raise. That amount is higher for the most junior enlisted. Imagine the value it has to an 82-year-old widow on a fixed income, or the wounded warrior and family trying to get back on their feet and find a new normal.

In times of austerity, we should not be looking to cut a benefit that the currently serving, wounded, widows, and retirees so greatly rely upon and earned access to when we can't afford to replace it with something equally good or better.

We are gratified that the Department of Defense has heard the call from patrons and recognized that the savings is the benefit, and higher prices or surcharges will hurt them or make them stop shopping at the commissary altogether.

DOD says it is focused on maintaining the patron benefit. We hope this includes using DeCA's current market basket calculation methods for savings. It is important to not reinvent what patron benefit is. If DOD uses new metrics to determine a current savings levels that will be used as metric going forward, we will not be measuring apples to apples. DeCA currently compares thousands of items in its market basket study against private grocers, and calculates an average savings of 30 percent. When Boston Consulting Group measured just 50 items in their market basket, it found a much lower savings level.

We believe changing the market basket study could result in a reduced benefit by excluding comparison of items commonly pur-

chased by patrons in calculating the savings measured. Therefore, maintaining consistency with previous calculations is imperative to maintaining the benefit that patrons know and rely on.

DeCA has been repeatedly asked to find efficiencies in providing this benefit, and they have done so. However, at some point, we think they will be forced to find them where it will be unpalatable to patrons either through price increases, changes in service, or changes in quality.

The cut to the second destination transportation subsidy in Asia last year recently demonstrated the potential costs passed on to patrons, with a bag of romaine lettuce costing more than \$10 in Guam. Those stationed overseas at the pleasure of their government should not be stuck with the bill for shipping resources to their location.

Proposals to merge the commissary and the exchanges are common. Most have not occurred, because it is difficult when businesses use different backroom logistics, different business goals, and operating restrictions. We simply don't know what we don't know. How will this affect product quality, savings, and customer satisfaction levels? If for the worse, how will that affect foot traffic for the exchange, affecting MWR dividends, affecting patron trust, access, and sustainment of support and quality-of-life programs? How will this impact the employment and earning power of approximately 10,000 military-affiliated employees, including more than 4,000 military spouses?

Maintaining the benefit at levels patrons can depend on, provide quality products, customer satisfaction and savings, with accessible hours and service should be the priority, and we thank this committee for outlining those benchmarks in the National Defense Authorization Act. We think those benchmarks are the best metric, which all new proposals should be evaluated against.

Thank you for this opportunity to share the views of MOAA and its members. I am happy to answer any of your questions, and I yield the rest of my time.

[The prepared statement of Ms. Goldberg can be found in the Appendix on page 95.]

Dr. HECK. Great. Thank you all very much for your testimony and for all of you staying within the 5-minute timeframe. I think it is the first for this panel.

I will ask Ms. Huck and Ms. Goldberg first. The committee has heard from DOD that military families desire the option of purchasing a private label product from their commissaries, and the studies done by BCG recommended that commissaries should offer private label products. Since private label products are uniformly offered in retail grocery outlets, do you believe that military patrons should be afforded the same choice as outside the gate, and why or why not?

Ms. HUCK. Mr. Chairman, our concern is that DeCA does not have the expertise to develop a private label product, and we are concerned about what the extra expenses and logistical responsibilities would be incurred if DeCA were to be required to provide a private label product.

Right now the commissary sells name brand items that patrons are familiar with and they have the assurance that those items are

of high quality and low cost. We are concerned that asking DeCA to develop a private label product would not give patrons that same assurance of quality.

Dr. HECK. Okay. Ms. Goldberg.

Ms. GOLDBERG. I think that Eileen covered all of the things that I also would cover.

Dr. HECK. Great. Thank you.

I will ask Mr. Nixon and Mr. Gordy. I understand that you both, both organizations have concerns and disagreements with some of the BCG findings. If you could list your top one or two concerns with a particular finding, please do so.

Mr. NIXON. Quickly, Mr. Chairman, I would characterize the results from the BCG report as kind of the good, the bad, and the ugly. Their pricing survey was certainly very limited when you consider that the Defense Commissary Agency does a full comparison item by item, UPC [Universal Product Code], weighted by volume, regionalized, they do local surveys on meat and produce to calculate the 30 percent savings. So it was kind of disingenuous to go out and take a small sample and come back and say here is more what the savings range is.

The other thing is they really kind of almost talked with disdain about the nonretail aspects of the Defense Commissary Agency, that, you know, they have these anomalies of vendor stocking and contracted-out functions within the store. The fact is that is the way Congress constructed the system, that is the way DOD conducted it, and it has a lot of difference anomalies to it that are built-in inefficiencies because it is a Federal agency. They, you know, they have inherently nongovernmental function surveys. They went through the A-76 process, outsourced a lot of their functions, shelf stocking, receiving, storage and handling, custodial. A lot of those are awarded at a premium under Javits-Wagner-O'Day, so it costs more to operate in the environment.

So in a retail operation, you would never operate a store that way. I think the BCG kind of missed that, that they are doing what they are doing because that is how they were set up to operate. There are more efficient ways to do it if you want to make them a retailer, but you need to make them a retailer first.

Dr. HECK. Mr. Gordy.

Mr. GORDY. I would say the top two items of concern for us related to the BCG report would be the private label products and variable pricing.

First of all, the private label product, the main concern there is currently you have name brand products being put into the stores, and for those products to get into that store, as Mr. Nixon said in his opening testimony, there is about \$500 million of industry support that goes to ensure that those products are stocked. Well, first of all, that they are ordered, that they are stocked, that they are marketed, that they are promoted. These are activities that take place in every commissary every single day that is funded by industry.

To institute a private label product is going to have two effects: number one, DeCA is now going to have to—what makes private label successful in the civilian marketplace is the amount of actual marketing that goes into getting the patron to buy those products.

So DeCA is now going to have to add to their cost and add to their staffing people who have to go out and market these products. Then they are also going to have somebody stock those products. And then they will have someone go in there and then they will have to do the promotions and the other—the displays and things like that to get the patrons to buy them.

Well, if DeCA is now going to take on those functions within the store, which is currently being provided by industry today, and these products are going to compete with the national brands, the national brand manufacturers are going to say, if DeCA is now going to provide this in-store support, which we are currently providing today, which we don't provide to any other retailer, then we are no longer going to provide it for DeCA.

So that is a conversation that has not taken place. No one has asked the manufacturers what will change. If you look at the BCG report, they list all the people that they consulted. They did not consult the industry, who are the third leg of the three-legged stool of delivery of this benefit. So they are missing a major piece of the pie here.

And in order to make variable pricing work within the commissary, they are going to have to institute variable pricing, which allows DeCA now to raise prices on products. This becomes a slippery slope. Today DOD can say, we are going to keep our hands tightly held on this and we are only going to do what—generate enough revenue just to help offset a little bit of cost. We don't know what will happen 5 to 10 years from now with the future leaders within DOD.

Dr. HECK. Thank you. Thanks very much.

Mrs. Davis.

Mrs. DAVIS. Thank you, Mr. Chairman. And perhaps I can continue with this conversation a little bit about the labeling, because I do remember in sitting here, you know, as a consumer when we had this discussion with BCG, we know that, you know, we all adopt, if you will, certain companies now and have some faith in their label. So you know, it seemed like, well, okay, you know, I think our military families, and you would subscribe to this, certainly have faith in the commissary. I mean, they have great faith in the commissary. They would transfer that in some ways.

But on the other hand, I hear exactly what you are saying. And I was struck that, Ms. Huck, you were saying that they don't have the expertise. It is not that they don't have the wherewithal to have the expertise, but the system hasn't been set up that way, and so there is really a gap there.

I think what I am wondering is how if you were tasked with trying to develop a process, and because it would be over time, to test this on a number of ways in which you were consulted and you were part of that, how would you do that? What do you think that we should be listening out for if, in fact, people say, you know, let's give it a try?

Mr. NIXON. I would say the first thing is a business system. This pricing model requires a sophisticated business system to manage price elasticity between the brand name and private labels and things that patrons are used to seeing out in the private sector. That system is currently being deployed at the Defense Com-

missary Agency. The first model that would give them the capability to even begin to look at this capability will be probably in the third quarter of this year.

So they will just begin to have the capability then. They will have to start testing it. As with any system deployment, if it is delayed, then that capability is delayed. That is the first thing, because you can't do this on a pencil and paper. And so they need the system. They will have that in place.

Mrs. DAVIS. Have you all been consulted about developing that system?

Mr. NIXON. This is a system that they procured through the government process. It is a commercial off-the-shelf. I don't have any qualms about the system. And it is replacing a lot of antiquated systems they had down there when I was down there, so they finally got around to replacing those. And then the expertise, it is not just the system, it is the expertise to manage in that environment. And they don't have it. And it is not their fault—

Mrs. DAVIS. Right.

Mr. NIXON [continuing]. They just weren't constructed to manage in that environment. So those are capabilities.

But, my concern is they are going to bring in—you know, we are going to figure out, well, how do we do variable pricing and private label? They don't know. They'll bring a consultant in that says, well, here is how you raise prices, and here is my bill and make sure you raise them high enough to pay it. You know, that it is kind of the path we are going on right now. It will take a while for them to develop that capability.

Mrs. DAVIS. Thank you.

Mr. GORDY. Absolutely. You know, even if you take a look at the Boston Consulting Group's report, they lay out that DeCA is going to have to first bring in a manager, and then they are going to have to bring in analysts to manage—the way that they characterize it is you need one analyst for every two categories, and there are numerous categories within the commissary. So how many of these analysts are going to be required to be able to do this?

Then you have to manage the savings. The way the savings, according to their survey, they went outside the gate at some commissaries, particular ones, and they measured the price of goods around each base that they tested. Well, you can't do that at every single base. How much time and effort is that going to take to maintain that level of savings comparatively to outside the gate at each base?

So some of the challenge of price rationalization, particularly trying to raise prices in certain parts of the country and then lower it in other parts of the country, that is going to take a lot of work to be able to pull off.

Mrs. DAVIS. Yeah. I appreciate that, Mr. Gordy. Thank you.

I am just wondering just in terms of the delivery and to families and, you know, the decisions that people make, of course, every day, and sometimes it takes a period of time for people to, like, transfer their loyalty, what is it about that delivery to families that you think especially needs attention?

Ms. GOLDBERG. I think there are a few things—

Mrs. DAVIS. Given that maybe all—some of these—you know, so many of these very important contingencies and issues would be worked out.

Ms. GOLDBERG. Are you asking specifically about private label and variable pricing? I think that any time you mess with the savings level, any time that families perceive that there is a threat to the savings that they receive when they go in the door, and an alteration to the delivery of the system, that you risk their loyalty. They really rely on knowing exactly what they are getting when they walk through that door, whether that door is at Stuttgart or in Guam or near Seattle or at Fort Sill. They rely on that consistency.

And so when you change things, you risk them leaving and not coming back, which then affects a whole lot of other systems that we rely on to support our military families.

Mrs. DAVIS. Okay. I think my time is up, Ms. Huck. Maybe we will follow up later. Thank you.

Dr. HECK. Mr. Walz.

Mr. WALZ. Thank you, Chairman, for holding this. And thank each of you for being here and your testimony of what you do. I think about it, with all the stress of military life, grocery shopping should not be one of them. And thanks to all of you, it hasn't been, and I think that is very important to keep in mind.

I think you started to hit on that, Ms. Goldberg is hitting on it, of all the things involved in it, that there is a strong psychological benefit here, and I think we need to again, I don't say that justify wastefulness where we can find efficiencies; I say it because it is a reality of military life. So I appreciate that. And I think it is probably because of the due diligence of the chairman and the ranking member of thinking about this.

And I don't know if this means anything or not, but since I have been on this committee, I have had more opportunity to look for cost savings in the commissary than the F-35, and that is somewhat—it is a little chip on my shoulder about that. If we are looking for cost savings, there is other places, but I do think it is right to look at these things and ask. And I think you are asking all the right questions with—

Ms. Goldberg, how would you—and I know maybe you can't quantify it. How high would you say, because I am thinking about this, how do we explain to the civilian sector how important the commissary is? How high do your members place the commissary benefit?

Ms. GOLDBERG. I don't have a specific numerical answer for you, but consistently when MOAA has surveyed its members, and other advocacy groups as well, there have been lots of studies on this, service members and their families, retirees rank the commissary very high, one of their most favorite benefits, along with health care. It is critical.

Mr. WALZ. I find myself talking to civilian people not quite understanding what our obsession is with the grocery store, but it is real, and especially—and I ask you this: are we getting into the wrong territory here if we separate CONUS [contiguous United States] with OCONUS [outside the continental United States] on the benefit of it, because I think that psychological effect is even

stronger overseas? And I am asking, is there things we can do here because of the availability of private sector, or is that the wrong way to go about it?

Ms. GOLDBERG. I agree that the need for commissaries OCONUS is very, very obvious. And there are a lot of questions about CONUS, but the reliance on commissaries stateside is still very, very important. Families rely on it. It is not just a grocery store. It is a place where military families meet up, whether they are in a high density area or a very remote area.

Here in the DC area, military families are spread out all over the National Capital Region, but the commissary is one place where they have in common.

And the price matching, or the price—not the price matching, but the price savings on goods is really, really critical. I have tons of grocery shopping choices. When I moved here, I will tell you, I was shocked when a package of bacon cost \$8 at my local private grocery store, but I went to the commissary, and it was roughly the same price it had been at the commissary that I went to in Florida. That mattered.

Mr. WALZ. Yeah it does matter. And I think all of you are hitting on something. Again, it is not stuck in that not afraid of change type of issue, but I still am not sure, and I think each of you hit on this, the unintended consequences of a change like this have not been studied, and I think there is a willingness to put it into a ledger sheet and a business model and say this is how it is going to turn out, and I worry about that, because, again, as I said, of all those stresses of military life, consistency on certain things is absolutely critical for those families.

And I would come back to that hit on the employment piece and maybe—I am not sure if this is the right group to talk to on this, the MWR funds and all that, this piece gets left out of that too, and as a senior enlisted soldier, how critical that is on where that—that is going to have be made up somewhere, and I am really not interested in watching our soldier's family do bake sales to fund, you know, ski rentals or whatever it might be. So I do think—and I ask my colleagues to take that into consideration, maybe asking the industry folks to do a little bit better about that. With those BCG recommendations, how does it affect your business model? I mean, can you summarize? What is going to change, the top line things that will change?

Mr. NIXON. Obviously the first thing that I mentioned earlier and Mr. Gordy did as well is the level of industry support. Around \$500 million industry puts in annually to offset the cost of operations. A lot of it has a historical perspective from the standpoint of vendor stocking, but a lot of it is—you know, the difference in this model is all promotional dollars go to the shelf. You know, there aren't any fees skimmed off that are in the retail environment, slotting fees and other pools that money go into.

So a manufacturer has a certainty when they put a promotion together, that price goes into the shelf. It is the ultimate supply and demand economy. They are going head to head with their other brand name counterparts with competition on the shelf, and the patron decides what items stay and what items go.

When you start changing the model onto the private sector side, there is manipulation in what is on the shelf. The private label items are price-positioned and promoted by a retailer, because it is a house brand. And it is artificial patron preference, because they position them next to the brand name, whether they have any sale or not, because that is what they want to sell, because that is where they make their money.

Mr. WALZ. Don't you think it is interesting the first thing you come to, and it is very obvious in this industry, these are the things you hit on directly as the major influence, and yet that industry wasn't consulted as part of the discussion. Doesn't that seem like a glaring hole? I know you mentioned it, but I am fascinated, because I kind of anticipated this was going to be your answer. The biggest thing that is going to change, that part wasn't taken in.

Mr. NIXON. Yes, sir.

Mr. WALZ. All right. I yield back.

Dr. HECK. Thank you.

Ms. Stefanik.

Ms. STEFANIK. Thank you, Mr. Chairman. And thank you to the witnesses for your testimony today.

I want to address my first question to Ms. Huck and Ms. Goldberg to further delve into the impact on military families. So I represent Fort Drum, where the military resale benefit is such an important fabric of the military community.

You, Ms. Goldberg, talked about, very articulately, that the goal should not be maximizing revenue; the benefit are the savings for our military families. What are the secondary and tertiary effects that weren't included in the BCG report or weren't included in the panel today of the impact of this proposed reorganization?

Ms. GOLDBERG. Thank you for your question. We talked about it a little bit in our statement for the record, along with my testimony. The interlocking mechanism of the commissary and the exchange is a very fine-tuned, harmonic relationship. The commissary brings foot traffic to the exchange. The exchange is another gathering place for people that operates with a profit margin that provides dividends to Morale, Welfare, and Recreation activities on the installation, and those could fund a variety of programs, and it is really critical to providing extra support and quality-of-life programs to military families.

When you start to take that apart and they lose faith in the commissary benefit, they might not go to the exchange. That reduces the dividends. That reduces the programs. All of a sudden military families may feel that there really aren't support programs for them anymore or that those programs are not important or valued by the Department of Defense or their community. And that really is a morale, I mean, it is detrimental to morale and readiness, and that is not a place, I think, that we want to go.

Ms. STEFANIK. Ms. Huck.

Ms. HUCK. I would add that the system is very interdependent in the sense that the large commissaries with a lot of volume help support economies of scale that support commissaries overseas and in remote locations here in the United States. And so our concern is that any change to the system that makes families less likely to

use the commissaries in these locations, such as here in the National Capital Region, will lead to less revenue available to support those commissaries in locations where families not only rely on the savings, but rely on the physical aspect of the store on the installation.

There are many locations even here in the United States and certainly overseas where families have few shopping options and certainly few affordable shopping options, and so we are very concerned about how any change to the commissary system will affect those families who are in locations where the physical presence of the store is critical to their well-being.

Ms. STEFANIK. Thank you. I also wanted to just note that I think one of the most significant statements that has been made from the panel is what Ms. Goldberg said, that these savings account for a 2 percent to a 9 percent pay raise for our military families. That is significant in these challenging economic times.

I want to turn to Mr. Gordy and Mr. Nixon. BCG, obviously one of their proposals was a private label. And Ms. Huck pointed out the fact that DeCA does not have the experience, the expertise, let alone the logistics capabilities. Can you elaborate on that and the challenges that would provide and the logistical issues that we would have to overcome to make that transition?

Mr. NIXON. Yes, ma'am. First of all, just to kind of set the playing field. DeCA did not introduce private label not because it didn't want to. Prior to last year's change in the law, there was a brand name exception to the Competition and Contracting Act, and so if you bought brand name products directly from a manufacturer, you didn't have to compete each order, but it developed into the signature of the commissary system is, was brand name and those brand names were found everywhere in the world that you went.

Private label is a company developed and supported brand. And we talked about they don't have the expertise to develop their own private label. DeCA is not big enough to develop a private label. They just—you know, it wouldn't be cost-effective, they wouldn't be able to manage the quality. So they will buy someone else's private label and put it in the store, but as a house brand, then they must price it, they must promote it, they must position it. And it is artificial positioning.

You know, the day it is put in the store, it doesn't have customer preference. They are going to give it artificial customer preference, because they want to sell it because they are making money on it. And that is primarily what private label does in the private sector.

So, yes, you can get from here to there. It is eyes wide open. Make sure we understand what is going on when we move into this environment and what actually is taking place is they are putting a brand in with artificial preference to mark it up to make money.

Ms. STEFANIK. Thank you. My time has expired.

Dr. HECK. Mr. O'Rourke.

Mr. O'ROURKE. Thank you, Mr. Chairman. This is my fourth or fifth hearing or briefing or roundtable on this issue in addition to the excellent briefing and background work that my staff has done, and I feel like I am just beginning to scratch the surface of an issue that is far more complex than it appeared at the outset.

And, for example, Ms. Goldberg, I have really been looking at the numbers and those things that we can measure, but you brought up a really important point: there is a social dynamic to this, there is a quality-of-life aspect that is perhaps immeasurable. You talked about military families having a secure, consistent place where they can meet and be with each other and share something that is unique to service, and I think that is important and something that needs to factor into our decisions and calculations.

But I would like, with the 4 minutes that remain, for each of you to take a minute—I am probably never going to achieve the depth that you have on this subject. Mr. Gordy, you mentioned that as we move forward, we should look at this as a game of inches. Mr. Nixon, you talked about ensuring that we measure this appropriately as we pilot things. Ms. Huck, you talked about apples to oranges. Can you just take a minute and tell me and the committee what we should be measuring going forward? What are the key measures or metrics, understanding we won't get all the quality-of-life aspects, that will tell us whether the changes that are coming forward are working or not?

And, Mr. Gordy, it looks like you are ready. We will start with you.

Mr. GORDY. Sure. You know, what is really interesting about this is why we are here, it has all been driven by the budget, and so much of what is in DeCA's budget are things that DeCA will never be able to make more efficient, because it is money that they give to other programs within the Department of Defense, such as on-base support, which they can't control how efficient those things are or whether or not those costs get reduced.

I think if we are going to change the model from what we have today from having national name brand products at cost plus 6 percent—1 percent for spoilage, 5 percent for surcharge—if we are going to abandon that model to move to a more complex model, we need to make sure that we have covered every area and understand every potential cost and every potential risk that might be faced as we move forward.

Not say that these things shouldn't be tested, but they should be tested in small bits, and making sure that if these things start to fail, that we pull back. So that would be my—

Mr. O'ROURKE. Let me ask Mr. Nixon, is—the Walmart golden rule of don't aggravate the customer seems to be very important. Would that be the primary metric, customer satisfaction, in the commissaries?

Mr. NIXON. Absolutely. One of the benchmarks I said was customer confidence, and clearly customer confidence is very high in the system right now because it is predictable. Everyone knows it is goods at cost, everyone knows what the surcharge goes for. When you start tweaking that and people no longer know exactly what is going where, what has been marked up, and why are these new products in that don't have demonstrated customer preference, why are they showing up, you start changing customer confidence, you start changing the predictability of the system.

And I think that is the benchmark of the system right now, it is predictability and the fact that its savings are audited—it is the patron satisfaction is done independently, and it is a valued store,

and it is viewed as their store, and we have to keep that in mind. This is that—the Defense Commissary Agency is managing their store.

Mr. O'ROURKE. And for Ms. Huck and Ms. Goldberg, I have about a minute left, does customer satisfaction get to some of the issues you raised, Ms. Goldberg, that might reflect military families' understanding of the value of those commissaries, if we are measuring that?

And, Ms. Huck, if there is time remaining, what are the apples-to-apples comparison we want to look at?

Ms. GOLDBERG. I don't know that I would rate savings, quality, or customer satisfaction against each other. I think they are all equally critical and they play an important role, and this committee really hit the nail on the head in setting those as benchmarks for measuring how this benefit is treated going forward, knowing that a decrease in any single one of those areas could really start dissecting the entire system and making it fall apart.

Ms. HUCK. I would add that we are very focused on transparency when it comes to making any changes to the commissary system. Right now, as Mr. Gordy and Mr. Nixon have pointed out, the system as it is structured is very clear. Families understand essentially how items are priced.

Any changes to that that are not clear to families, I think, is going to really inspire a lack of confidence in the system and the quality in the store that right now they rely upon. So we are asking for transparency in any changes that DOD makes moving forward.

Mr. O'ROURKE. Thank you. Thank you for your answers.

Mr. Chairman, I yield back.

Dr. HECK. Mr. MacArthur.

Mr. MACARTHUR. Thank you, Mr. Chairman.

Thank you for being here. You have all very ably represented your members, and I was struck by one thing that each of you said. Mr. Nixon, that we need to avoid this trap that the beatings will continue until morale improves; Mr. Gordy, that we should avoid aggravating our customers; Ms. Goldberg, that this is the single highest valued benefit that members identify; and, Ms. Huck, that those overseas at the pleasure of their government should not foot the bill. And I think for me, those are all pretty important measures of how we should approach this.

I would associate myself with some of Mr. Walz's comments, not the F-35 comment, but grocery shopping should not become stressful when we have got a lot of other issues that our military families have to deal with.

And before I pose a question, there are three things I think we should remember. One, we have had these four or five hearings now, and we are talking about how many hundredths of 1 percent of the military budget we can save, and I think we have to keep that perspective. We are talking about a lot of dollars, but relatively a very, very small percentage of our defense budget.

And, two, that the benefit to our service members goes beyond just the commissary benefit. Ms. Goldberg, you have mentioned—and I got your quotes backwards, actually, but you recognized that as I said it. But there are other benefits that come from this com-

missary benefit than just financial, and there are other benefits to the U.S. economy. It benefits our service members, it also benefits U.S. suppliers, it benefits the U.S. economy, and any changes have downstream effects.

And, thirdly, we are about to consider meaningful changes to the healthcare system of our service members. And there is a compounding effect, I think, when we do too many things at one time, and so I think we need to be very cautious.

And that leads me to this question I would ask each of you. What improvements would you advocate to the system, the commissary system, that would not hurt morale, that would not cause aggravation, that would not be seen as a decline in benefits, and that wouldn't ruin the downstream benefits that you have described? In other words, what changes do you see that cause no harm to this system?

Mr. NIXON. Well, yes, sir. That is an excellent question. And I would say that—and I think because many of the things that are in the back office environment fall into the too-hard-to-do box initially, they focused on the front end of something that is a little easier to do, and so I think that is where the focus is. I think there are so many things that can be done on the back end.

You know, these are all business environments that order computers, supplies, store supplies, consulting contracts, major systems award, these are all business systems that manage inventory and throughput and front-end systems. I would probably look at—short of making DeCA a non-appropriated fund activity, is there an opportunity to loosen some of the procurement regulations on them to let them operate a little more in the quasi-government environment to let them participate with the other business operations, and—

Mr. MACARTHUR. I am going to stop you there. I get the point, and it is a good one.

Mr. Gordy.

Mr. GORDY. I would just have to echo what he was saying, Mr. Nixon was saying. I mean, if you take a look at the exchanges, the—particularly AP's just went through a restructuring, they were looking at about having a \$50 million dividend. They went through a restructuring. Their dividend is now back in the—or remained in the \$200 million level, or close to that. So there are things that can be done inhouse that have no impact. It is just about running it more efficiently. So—

Mr. MACARTHUR. And, Ms. Huck, we have got just about 45 seconds more.

Ms. HUCK. I would answer what we would ask you not to do, which is make changes that affect the shopping experience for the military family and the service members who shop there. There are certainly efficiencies that can occur at the—above the store level that might make the system run more efficiently, and we would certainly be open to that, but anything that affects the shopping experience of the military family or service member, we think the value—the quality of the shopping experience itself and the access in terms of operating hours is an important part of the benefit.

Mr. MACARTHUR. And Ms. Goldberg.

Ms. GOLDBERG. I concur with the previous statements, that the changes should be relatively invisible to the patron, unless they are improvements.

Mr. MACARTHUR. All right. Thank you all.

I yield back.

Dr. HECK. Mr. Coffman.

Mr. COFFMAN. Thank you, Mr. Chairman.

Well, I have somewhat of a different view. First of all, let me just say thank you all for supporting our military families. I have 21 years combined military service, Active Duty, enlisted, United States Army, infantry officer of the United States Marine Corps, five overseas deployments.

I support these reforms. And I think that they are not going to compromise the benefit for our families. But they are threatening for the people who run the system, and I understand that, and change is always difficult. And so if you—in your opposition, I really strongly suggest and would love to hear more about your ideas to make this system more efficient. We have got to challenge government everywhere. We have got to challenge government to be more—you know, to be able to deliver services more efficiently, and no area of government ought to be immune from that, and so that is my concern. And I challenge you all to do that.

Mr. Chairman, I yield back.

Dr. HECK. Thank you.

You know, I understand that there certainly is the monetary savings is critically important, and I think the points that have been brought up about making sure we have the correct market basket and the correct analysis is critically important. As you mentioned, Ms. Goldberg, DeCA talks about a 30 percent savings, the BCG group with their modified basket had it somewhere around 20 percent or a little bit less.

Needless to say, there is a break point at which if there is not enough savings, people are going to walk. So for the sake of argument, let's say we want to maintain—we set a benchmark that the market basket savings has to be 30 percent. If variable pricing allows that 30 percent savings to be maintained over what is available outside the gate, whether you are shopping in a high-priced area or a lower priced area in the economy, as long as the service member and their family is getting that 30 percent savings over what is available outside the gate, what would be the downside to the pilot program of trying variable pricing? Ms. Goldberg.

Ms. GOLDBERG. I would defer to the business mechanics of that to the colleagues at the other end of the table, but as long as the savings is maintained and when the customer walks in the door, they receive that same consistent benefit, whether that commissary is in a remote location or overseas or in a high-density area, I don't see a downside as long as we can maintain that savings and not have the fallout of lost employees and other issues that could affect other military members.

Dr. HECK. Ms. Huck.

Ms. HUCK. Mr. Chairman, I would say that Brooke actually made the point in her statement earlier that she had the confidence when she moved here to a high-cost area that the cost of her groceries would be the same here as it was when she lived in Florida.

And that is our concern when we talk about variable pricing and setting the savings level based on what is available outside the gate versus a national standard, you run the risk that families in high-cost areas are actually going to ultimately be paying more, because the 30 percent of the cost in the DC area is a different value than 30 percent when you are talking about a lower cost area.

So part of, I think, what makes the commissary so appealing right now to families is that reassurance that wherever they go, the prices are going to be consistent, and we would be concerned about anything that might potentially take that assurance away from families.

Dr. HECK. And so I would ask, is that a reasonable expectation that if you are living in San Francisco, you are going to pay the same amount for a grocery that you might be purchasing if you live in Tupelo, Mississippi? I mean, just for the sake, you know—again, the idea is that the level of savings should be based upon maintaining the foot traffic in the commissary, which means there has to be a savings over what that person would spend if they go outside the gate.

Ms. HUCK. Our concern would be that the pay, leaving housing allowance out of the equation, your pay is the same whether you are in Tupelo, Mississippi, or in San Diego. And so we don't want to see families who are in high-cost areas put at a disadvantage.

Dr. HECK. Okay. Mr. Gordy.

Mr. GORDY. Mr. Chairman, the way, you know, I look at the price rationalization is, again, you are going to have winners and losers, and in the areas where there is going to be the loser, people that, for instance, here in the Northern Virginia area, people in the San Diego area, people in Pearl Harbor, they are going to see the cost of the products go up.

Now, most of us have a grocery budget, right? If the prices go up in the commissary doesn't mean our budget goes up; it means we still spend the same amount of money on groceries whether, you know, if something is 5 percent higher or whether it is 5 percent lower. That budget is the budget.

For the families in these higher cost areas, they are going to end up having to—they are going to end up buying less, and that is part of the challenge, in these areas, where BCG said even a 5 percent price increase will result in a 26 percent reduction in traffic. So we have to measure, if we are going to increase the price 1 percent, 2 percent, 3 percent, what is going to be the adverse impact.

And then when they also talk about rationalizing prices across categories. Now, I will tell you, I came and dropped my testimony off on Monday. I was on my way home. I said, oh, I am near Fort Myer, let me pop into the commissary. I called my wife, what do we need? She said stock up on meat. And they are talking about raising prices on meat. My wife knows, if there wasn't a good deal on meat, she wouldn't tell me to stop at the commissary and do that, but that is what a lot of military families do, they stock up at the commissaries.

And if the prices go up in these high-cost areas and it doesn't make sense to drive, for me it is 27 miles to the nearest commissary from my house, and my wife and I—every 2 months we go to a commissary and we stock up. We bought a freezer for that pur-

pose. If the prices go up, it doesn't make it worth the trip anymore. And so that is the challenge that many military families are going to have to—that is the question that they are going to have to ask themselves, is it now worth the trip.

Dr. HECK. My time has expired.

Mrs. Davis, any other questions?

Mrs. DAVIS. Oh, thank you, Mr. Chairman. And I know that the votes have started.

The one thing I would just want to add to this discussion, I think, and I was telling the—actually, I think San Diego is cheaper than here, at least when I go to the grocery store, but fresh fruits and vegetables, I mean, that is what we really want our families to access, and to use farm products from local areas. And I know when you are overseas certainly—I guess in Japan, I don't know that I had a lot of fresh fruits and vegetables, but I am just trying to make sure that we throw that into the discussion and that we ask some appropriate questions about that too so that our families really know that that is important.

And I don't know that there would be anything different around there. It is not a labeling issue. It is not something where, you know, families have said, that is something that we are willing to consider, again, given the right kind of studies that are done to look at that issue, but I certainly want to be sure that we don't, you know, eliminate all the issues around fresh fruits and vegetables and the farm-to-table issues that are very important throughout the country and certainly very important to our military families. Thank you.

Dr. HECK. Well, since they have called votes, I want to thank our panel for taking the time to be here with us this morning and for your excellent testimony. Please, you know, stay in touch with the members of the subcommittee as we move forward. I want to assure everyone that our goal is to find efficiencies, create a benefit that is sustainable and valued by our service members. And we are all awaiting the GAO report and DOD's recommendations, and I am sure there will be another hearing once those come out. So, again, thank you all very much.

This meeting is adjourned.

[Whereupon, at 11:33 a.m., the subcommittee was adjourned.]

A P P E N D I X

JANUARY 13, 2016

PREPARED STATEMENTS SUBMITTED FOR THE RECORD

JANUARY 13, 2016

Opening Remarks – Chairman Heck
Military Personnel Subcommittee Hearing
Views on Commissary Reform
January 13, 2016

I want to welcome everyone to today's Military Personnel Subcommittee's hearing on commissary reform.

We are here today to hear from military service organizations and the grocery retail industry on the value of the commissary system to beneficiaries and the effects of any possible changes to the commissary's business model.

As we're all aware, commissary benefits are a valued part of our current and retired service member's compensation package, and contribute to their and their families overall quality of life.

The Military Personnel Subcommittee is taking every opportunity to thoroughly review and discuss the way forward on any commissary reform and is committed to retaining the commissary benefit while improving the business practices of the commissary system and at the same time reducing its dependence on appropriated funds.

Our purpose today is to gain an understanding from the panel on their views of the possible effects to the beneficiaries or to the business practices of our industry partners of any changes to the commissary system business model.

Before I introduce our panel, let me offer Congresswoman Davis an opportunity to make any opening remarks.

STATEMENT BY:

MR. PATRICK NIXON

PRESIDENT – AMERICAN LOGISTICS ASSOCIATION

BEFORE THE SUBCOMMITTEE ON PERSONNEL

COMMITTEE ON ARMED SERVICES

UNITED STATES HOUSE OF REPRESENTATIVES

2nd SESSION 114TH CONGRESS

January 13, 2016

**NOT FOR PUBLICATION
UNTIL RELEASED BY
HOUSE ARMED SERVICES COMMITTEE**

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.

Patrick B. Nixon**President, American Logistics Association**

Patrick B. Nixon is President of the **American Logistics Association (ALA)**, headquartered in Washington DC. The ALA is a voluntary, nonprofit organization of manufacturers, manufacturer's representatives, brokers, distributors, publishers, and other companies that sell or provide products and services to the military resale systems and MWR/Services. At ALA, we use the term "military resale systems" as a broad term that includes all military exchanges and commissaries, Department of State stores, Veterans Canteen Services, as well as all of the armed forces' Morale, Welfare, and Recreation (MWR) activities that involve a product or service. The ALA membership includes over 250 of America's leading manufacturers, nearly 60 brokers and distributors, service companies, media outlets and more than 1400 individual members. Mr. Nixon is responsible for articulating the association's positions on issues and programs to the membership, the Congress, DoD and military resale partners. He develops the legislative focus for the association and serves as the principal spokesperson for the ALA. In 2011 Mr. Nixon was recognized by the White House as a Champion of Change for extraordinary leadership in the hiring veterans and military family members

President, The Coalition to Save Our Military Shopping Benefit

Patrick B. Nixon is President of The Coalition to Save Our Military Shopping Benefits, headquartered in Washington DC. The Coalition is a voluntary, nonprofit organization of patrons of the military resale system, employees, manufacturers, manufacturer's representatives and concerned Americans that want to know more about this important quality of life benefit and protect it from unnecessary reductions. At the Coalition, we use the term "military resale systems" as a broad term that includes all military exchanges and commissaries, Department of State stores, Veterans Canteen Services, as well as all of the armed forces' Morale, Welfare, and Recreation (MWR) activities that involve a product or service. The focus of the Coalition is to educate, engage and excite members and non-members alike with key information about these valued benefits and provide a forum to protect them should they come under attack .Mr. Nixon is a recognized expert in the fields of military resale, international business and association management. In addition to his duties at the Coalition, Mr. Nixon serves as the President of the American Logistics Association. Mr. Nixon joined the American Logistics Association in 2007 and was one of the key architects in the establishment of the Coalition in 2011.

Member, Board of Directors

The Federation for Identity and Cross-Credentialing Systems

March 2011 – Present (4 years 8 months)

The Federation for Identity and Cross-Credentialing Systems (FiXs) is a coalition of commercial companies, government contractors, and not-for-profit organizations who have established and maintain a worldwide, interoperable identity and cross-credentialing network built on security, privacy, trust, standard operating rules, policies, and technical standards.

Defense Commissary Agency

Director and Chief Executive Officer

Government Agency; 10,001+ employees; Supermarkets industry

April 2004 – November 2007 (3 years 8 months)

Provided leadership and direction to the military's supermarket chain consisting of over 270 stores located in 14 different countries around the world. Annual sales for the agency exceeded \$6 Billion and the workforce consisted of over 18,000 employees. Recognized by the Secretary of Defense and the President for exceptional leadership and dedication.

Defense Commissary Agency

Chief Executive Officer

Government Agency; 10,001+ employees; Supermarkets industry

June 2001 – April 2004 (2 years 11 months)

Directed daily operations of the military's supermarket chain consisting of 270 stores, 18,000 employees and annual sales exceeding \$6 Billion.

Defense Commissary Agency

Senior Management Positions

January 1991- March 1993 Director Southwest Region

March 1993- March 1996 Director Northeast Region

March 1996- June 2000 Deputy Director European Region

June 2000 – June 2001 Director Eastern Region (Promoted to Senior Executive Service)

United States Marine Corps

Enlisted Marine

Government Agency; 10,001+ employees; Military industry

June 1966 – August 1969 (3 years 3 months)

Served as an Enlisted Marine assigned to the 27th Marine Regiment, 5th Marine Division. Transferred under the November 1967 rotation to the 1st Marine Division, Danang RVN

Military Awards

Navy Achievement Medal with "V" device for valor

Presidential Unit Citation 1st Marine Division RVN

Navy Marine Corps Good Conduct Medal

National Defense Service Ribbon

Vietnam Service medal

Vietnam Campaign Medal with 3 stars

Vietnamese Cross of Gallantry

Rifle & Pistol Expert

Education:

1972, Bachelor of Arts degree in philosophy and political theory (cum laude), University of Maryland, College Park, Md.

2005 MBA Tulane University Freeman School of Business

1978, juris doctor degree, University of Baltimore School of Law, Md.

Graduate studies, European Institute of Public Administration, Brussels, Belgium

Graduate Studies, Harvard's John F. Kennedy School of Government, Cambridge, Mass.

Advanced studies certificates in corporate governance, Tulane University School of Law and Freeman School of Business, New Orleans, La.

Executive study sessions, Brookings Institute, Washington, D.C.

AWARDS AND HONORS:

White House Champion of Change (2011-2012)

Presidential Rank Award for Meritorious Senior Executives and Professionals

Secretary of Defense Medal for Meritorious Civilian Service

Senior Executive Service Exceptional Performance Award

National Industries for the Blind "Visionary Award" 2006/2007

National Military Families Association's Anna Chenault Award for Exceptional Support to the Military Family

Defense Commissary Agency's Distinguished Civilian Service Award

DeCA Meritorious Civilian Service Award (4 Awards)

U.S. Navy Meritorious Civilian Service Award

U.S. Army Commanders Award for Civilian Service

**DISCLOSURE FORM FOR WITNESSES
COMMITTEE ON ARMED SERVICES
U.S. HOUSE OF REPRESENTATIVES**

INSTRUCTION TO WITNESSES: Rule 11, clause 2(g)(5), of the Rules of the U.S. House of Representatives for the 114th Congress requires nongovernmental witnesses appearing before House committees to include in their written statements a curriculum vitae and a disclosure of the amount and source of any federal contracts or grants (including subcontracts and subgrants), or contracts or payments originating with a foreign government, received during the current and two previous calendar years either by the witness or by an entity represented by the witness and related to the subject matter of the hearing. This form is intended to assist witnesses appearing before the House Committee on Armed Services in complying with the House rule. Please note that a copy of these statements, with appropriate redactions to protect the witness's personal privacy (including home address and phone number) will be made publicly available in electronic form not later than one day after the witness's appearance before the committee. Witnesses may list additional grants, contracts, or payments on additional sheets, if necessary.

Witness name: Patrick B. Nixon

Capacity in which appearing: (check one)

Individual

Representative

If appearing in a representative capacity, name of the company, association or other entity being represented: American Logistics Association

Federal Contract or Grant Information: If you or the entity you represent before the Committee on Armed Services has contracts (including subcontracts) or grants (including subgrants) with the federal government, please provide the following information:

2015

| Federal grant/ contract | Federal agency | Dollar value | Subject of contract or grant |
|----------------------------|----------------|--------------|---------------------------------|
| None | | | |
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2014

| Federal grant/ contract | Federal agency | Dollar value | Subject of contract or grant |
|----------------------------|----------------|--------------|---------------------------------|
| None | | | |
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2013

| Federal grant/ contract | Federal agency | Dollar value | Subject of contract or grant |
|----------------------------|----------------|--------------|---------------------------------|
| None | | | |
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Foreign Government Contract or Payment Information: If you or the entity you represent before the Committee on Armed Services has contracts or payments originating from a foreign government, please provide the following information:

2015

| Foreign contract/ payment | Foreign government | Dollar value | Subject of contract or payment |
|------------------------------|--------------------|--------------|-----------------------------------|
| None | | | |
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2014

| Foreign contract/ payment | Foreign government | Dollar value | Subject of contract or payment |
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| None | | | |
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1/11/2016

Statement of

Thomas T. Gordy

President

Armed Forces Marketing Council

before the

Subcommittee on Military Personnel

Committee on Armed Services

United States House of Representatives

January 13, 2016

Submitted for the record.

Not for publication until

released by the House

Armed Services Committee.

Chairman Heck, Ranking Member Davis, and Distinguished Members of the Personnel Subcommittee,

Thank you for your commitment to our Warriors and their families who continue to tirelessly serve and sacrifice in defense of our nation. And thank you for the opportunity to share views on behalf of the Armed Forces Marketing Council (AFMC) regarding efforts to reform the commissary benefit. In accordance with Rule XI, Clause 2(g)(5) of the Rules of the House of Representatives, a curriculum vitae and disclosure form are enclosed as exhibit 1.

As you are aware, to date there are no specific reforms that have been publicly proposed by the Department of Defense (DoD) since Congress passed and the President signed into law the FY16 National Defense Authorization Act (NDAA) last month. The FY16 NDAA requires the Department of Defense to submit to Congress by March 1, "a comprehensive plan to achieve by October 1, 2018, budget neutrality in the delivery of commissary and exchange benefits" while ensuring high levels of customer satisfaction, the provision of high quality products, and the sustainment of discount savings.

We are grateful to the Committee for establishing the benchmarks for any potential reform efforts. The AFMC has long held that while efficiencies and/or reform efforts are possible, they should not diminish the benefit to our military families. The AFMC also offers its appreciation to the Committee for continuing to fund the Defense Commissary Agency's (DeCA) budget despite proposals to severely reduce the budget ahead of efficiency efforts.

Simple Model vs. Complex Model

As we begin our discussion today, we believe it is helpful to remember that Congress established the commissary as a non-pay compensation benefit for military personnel. The model that Congress forged is one that is as brilliant as it is simple - offering products at cost plus 6% to provide military families, regardless of where our nation asks them to serve, a non-pay compensation through savings on grocery products. All stakeholders in the commissary benefit, whether a patron, DeCA employee, member of industry or Member of Congress, understand the brilliance and clarity of this approach.

While no specific formal proposals have been offered to the Committee, over the course of the past two years, suggestions have been offered for commissary reform by both the Military Compensation and Retirement Modernization Committee (MCRMC) and the Boston Consulting Group (BCG) that would alter the model. The suggestion call for a more complex operational model through untested and under-analyzed pricing schemes and adjustments to product assortment, which will require a growth in both personnel and operational costs. These new, additional costs will have to be offset by the schemes in order to result in efficiencies. Several of these schemes place emphasis on generating operating margin from the patron at the expense of the original intent - products at cost plus.

Since we do not anticipate that there will be increases in appropriations to cover these costs, the revenue will have to be generated, and it can come from only one source: the military family.

The suggestions that have been offered are based on assumptions that product and pricing schemes are manageable and would still offer a benefit to military families. But even the suggestions have a caveat that they need to be further analyzed. The AFMC agrees and believes that full-spectrum analysis should be conducted on all efforts that would change DeCA's fundamental mission and seek to generate revenue from military families.

The AFMC also believes that accountability for the commissary benefit should remain with Congress. However, it appears the FY16 language waives congressional oversight through the waiver of Title X for at least the next five to ten years during a test pilot period. We hope that, if test pilots begin to fail to meet established benchmarks and/or the benefit for families begins to diminish, and if the DoD fails to act in an expeditious manner to protect the benefit, that Congress will step in to protect the benefit for our military families.

We also hope that Congress will only allow permanent changes to Title X for those concepts that are proven to be beneficial and efficacious to the long-term viability of the commissary benefit.

Quality of Life Ecosystem

We should also bear in mind that the commissaries are one part of the military quality of life ecosystem on military bases. Joining them in that ecosystem are the military exchanges and Morale, Welfare and Recreation (MWR) programs. If the commissaries are adversely impacted by the reform efforts and patrons begin to abandon what they view as a diminished benefit, it will adversely impact foot traffic in the exchanges, resulting in sales declines, which then would result in a decline in MWR dividends produced in the exchanges.

Today, military patrons give commissaries and exchanges some of the highest customer satisfaction index scores in the retail industry and military patrons, regardless of where they are stationed around the world, have access to high-quality, name-brand products that they know and trust at a price that saves them money.

Today, military families continue to enjoy significant savings in both the commissaries and exchanges, which support their quality of life and financial readiness, and are part of the non-pay compensation benefit package promised to our military personnel. The savings provided to patrons is an exceptional return on investment on the appropriated dollars spent on its delivery. Additionally, the military exchanges continue to provide a significant dividend in support of MWR programs. We agree with Congress that any effort to reform the commissaries should also weigh impacts on the exchanges and MWR.

A Reasonable Approach to Efficiencies

While the budgetary pressures of on-going deficits and the sequester have forced the DoD to make painful cuts to numerous programs, we recognize that resale is not immune to the pursuit of efficiencies. The AFMC believes that efficiencies can be achieved within the commissary system and should occur as long as they do not result in higher prices and diminished benefits for military families.

Unfortunately, what we have seen over the past few years as DoD has repeatedly requested draconian cuts to DeCA's budget, the efficiencies touted were not efficiencies at all in that they did

very little to reduce cost of operations. Rather they either transferred the cost of operations on to military patrons through higher prices or they diminished access to the benefit through reduced store hours or store closures.

We agree with the newly-appointed Deputy Chief Management Officer Peter Levine that efficiencies should drive the budget. We are encouraged by this new approach within DoD, which mirrors how any reasonable organization would approach reform and efficiencies.

We also agree with Congress that the efficiencies should not undermine the benefit to military families by adversely affecting customer service, product assortment and selection, and savings. In addition, we further believe that access to the benefit should not be adversely impacted.

Rule No. 1 of Retail - Don't aggravate your customer

The AFMC approaches reform efforts cautiously due to recent adverse impacts on retailers stemming from small changes in business models and operations. Two examples include Wal-Mart's clean store policy, which called for fewer products in each category and less aisle clutter (resulted in a loss of nearly \$2 billion in sales^{1,2}), and J.C. Penney's attempt to offer everyday low prices to its customers (resulted in a devastating loss of sales³), both of which were costly to each retailer and resulted in the firing of senior leaders. They listened to their consultants, and even their customer surveys, but the changes ended up aggravating customers who either purchased less and/or shopped elsewhere.

The retail market place is very sensitive to change. As BCG discovered, even a 5% price increase on prices in the commissary would result in a 26% decrease in traffic. In other words, to generate \$143 million in revenue would cost DeCA \$1.333 billion in lost sales.⁴ That should serve as caution to anyone interested in commissary reform, that efforts should be fully analyzed and evaluated, and carefully implemented.

¹<http://adage.com/article/news/walmart-reversal-marks-victory-brands/142904/>

²<http://consumerist.com/2011/04/18/walmart-declutters-aisles-per-customer-request-then-loses-185-billion-in-sales/>

³ <http://www.investopedia.com/stock-analysis/043015/how-close-jc-penney-bankruptcy-jcp-kss.aspx>

⁴ Boston Consulting Group, page 109

As Lee Scott, former CEO and current board member of Wal-mart has said, "Rule No. 1 of retailing is don't aggravate your customer." The AFMC agrees. Unfortunately, some have learned this truth the hard way. We hope this will not be true for commissaries.

The AFMC believes reform efforts should be a game of inches - proceeding slowly and only implementing concepts that can easily be reversed if negative effects begin to occur.

Therefore, this testimony will seek to offer opinions and/or concerns regarding the requirements of the aforementioned FY16 NDAA-required report as well as other commissary/resale reform suggestions that have been proposed by the MCRMC and BCG. Since the suggested reforms are speculative at this point, the AFMC reserves the right to alter its opinion once specific proposals and implementation plans have been developed, proposed and evaluated.

Budget Neutrality

The AFMC believes that achieving budget neutrality, or zero appropriations, while maintaining the required benchmarks is impossible. Appropriated dollars will be required to deliver a commissary benefit that achieves high customer satisfaction, the provision of high-quality products and maintains the current level of savings for the military patron. Without the appropriation, prices will have to be raised to offset costs. The AFMC believes raising prices to offset DeCA's budget would set the benefit on a death spiral as higher prices result in a loss of sales which would then require cuts in service and/or additional price increases, resulting in the eventual closure of commissaries.

This is not without precedent. In the past, an attempt was made to have a self-sustaining commissary at Carswell Air Force Base which had been closed due to Base Realignment and Closure. The commissary was allowed to remain open but was managed like an exchange, selling items for profit to offset the costs. It was a dismal failure. Today the Carswell Commissary is back under DeCA control and operating and thriving as a full-fledged commissary.

Based upon that test, we do not believe commissaries will ever be self-sustaining and will require a sufficient level of appropriated support to maintain the savings benchmark.

Privatization

Privatization is a concept that has been reviewed on numerous occasions, including by the MCRMC, and was found to not be a viable option for delivering the benefit. The AFMC agrees. Any effort to pursue privatization further would be a waste of resources and manpower.

Resale Consolidation/Shared-Services

Historically, the AFMC has taken a position that resale consolidation, or consolidation of commissaries and exchanges into one resale organization, should only occur if a solid business case was presented that did not diminish the benefit for military patrons. Our position has not changed. To date, no such business case has been made, even after nearly \$20 million was spent on studies and task forces.

Based upon past studies, it is been made clear that consolidation is an expensive undertaking and would require significant upfront investments in financial resources. And since non-appropriated funds would be required to pay for consolidation, there likely would not be enough resources to pay for the consolidation as the costs would likely exceed the profits generated by the exchanges. That would result in no MWR dividend, requiring additional APF to offset the loss of dividends or the potential elimination of some MWR programs.

We understand, however, that shared services is a likely approach to finding savings and efficiencies. Granted, the shared services most likely would be among the exchanges, at least initially. We are concerned that NAF dollar savings from the exchanges would be funneled to offset commissary APF dollars. This would establish pressure on the exchanges to produce savings while DeCA would not be required to produce such savings. We believe that savings achieved by exchange efficiencies should remain with the exchanges and be used to reduce prices in the

exchanges and/or support quality of life programs in order to strengthen the benefit for military families.

We commend the exchanges for the efficiency efforts they have put in place in the past couple of years to reduce operational costs in the face of declining numbers of eligible patrons due to budget cuts and reductions in troop levels. As a result, though sales have declined, they have been able to strengthen the dividend for MWR programs.

Commissary Closures/Reduced Store Hours

We agree with BCG that increasing store hours, vice reducing them, would “strengthen DeCA’s value proposition” and make shopping at the commissary more convenient. Unfortunately, in previous efficiency efforts, DeCA reduced store hours and days of operations, as well as closed stores. Recent budget proposals called for further reductions in access to the benefit through this same practice.

If DeCA becomes dependent upon revenue generation to offset APF, it will need to make commissaries more accessible to patrons in order to grow sales and increase revenue. Reducing access to the benefit will only further erode the benefit and make it more difficult for DeCA to capture efficiencies.

We are also aware that, due to personnel turnover within DeCA, the commissary budget has been under executed for the past couple of years. Due to the gapped billets, service levels in the commissaries have been adversely impacted. We have been made aware that some commissaries have low staffing levels which result in long check-out lines. We hope to see a quicker hiring process that ensures sufficient staffing in the commissaries in order to maximize the service levels for our military families.

Private Label/Variable Pricing

In May 2014, the then-Vice Chairman of the Joint Chiefs of Staff testified before the Senate Armed Services Committee that if DeCA were able to carry “generic” products, more commonly referred to as private label, then DeCA could be more efficient. An example of Ibuprofen was used, claiming that DeCA only carried the name brand option, Advil, and that he could get a lower cost, “generic” option at the exchanges. However, the VCJCS was incorrect. In fact, the commissary carried a value brand option that was cheaper than any other private label brand offered. In fact, DeCA’s value brand had 47% Ibuprofen marketshare in the commissaries. Despite the false testimony by a senior DoD official, which was never corrected, private label has been offered as a panacea for DeCA’s budgetary woes. As a result, in the FY2015 NDAA, Title X was unfortunately amended to allow for private label products to be sold in the commissary.

Historically, the AFMC has opposed private label products in the commissary for numerous reasons. First, the commissary, through Congressional intent, is a name-brand benefit that offers national brands at cost-plus. That is what makes the commissary so appealing. Because these products are sold at cost-plus, even some of the tier 1 and tier 2 products are competitive with or cheaper than many private label brands outside of the gate. As such, DeCA developed its Value Brand Program which highlights those national brands that are priced the same or lower than the lowest priced similar items outside the gate. Instituting private label products in the commissary would displace these quality, national-brand value products with a private label product that may not be cheaper or of better quality than what is already offered.

There are important benefits associated with the national brand offering, such as:

- The products are widely distributed, promoted, and advertised. They are very popular with DeCA shoppers, as well as their civilian counterparts.
- National brands offer a familiar touch of home for military families. Wherever they are stationed, military families can buy the very same products to which they are accustomed and like.
- National brands offer a known, consistent standard of quality at a known value, offering commissary patrons the ability to gauge accurately the savings available to them at DeCA commissaries.

To implement a private label program is a complex undertaking that will require upfront costs to contract and develop products as well as additional ongoing costs to implement. And there will be additional costs to ship, stock, merchandise and promote the items - costs that are all paid by the vendor community today for the national brand items. As BCG points out, DeCA does not currently have the structure in place to fulfill all of the requirements to properly and effectively manage a private label program and would need to create the structure and hire additional people to manage the structure.⁵ These costs will come from APF dollars without the benefit of having sold a single product.

But what BCG does not identify is how willing industry partners will be to continue to provide the in-store ancillary support, support that is not provided to other retailers, if DeCA is now competing with them at the shelf and generating profits from the products. This support includes promotional trade spending, retail store support to include schematic sets, distributor management, promotional signage, shelf stocking, and working with stores to keep computer assisted ordering data accurate.

If industry no longer decides to pay for and conduct the in-store support, these costs will have to be borne by DeCA. As far as we can tell, these costs have not been factored into any of the analysis. In BCG's report, they list all of the people they consulted. Unfortunately, industry was not included in their list.⁶ Thus the AFMC believes their assumptions on revenue generation, lower product costs, and savings generated through the sale of private label products are flawed in that they did not take into consideration second and third order effects of introducing private label products in the commissaries.

Private label will change everything for everyone affiliated with delivering the commissary benefit. Pursuing private label requires a full-spectrum analysis which has yet to be conducted. Therefore, we believe further analysis is required to fully understand all of the costs associated with instituting private label before it is implemented.

It should be noted that many product recalls are related to private label products. Whole Foods and Wegman's, both of which are known for their private label products, had some of the highest number of recalls among retailers in the past two years. Overall, most product recalls are due to

⁵ Boston Consulting Group, page 124

⁶ Boston Consulting Group, page 17

undeclared ingredients, for instance, nuts and other allergens present in products that did not disclose the items were present, creating a grave danger for many who are allergic to those ingredients.⁷

Under the name brand program, DeCA bears no financial risk or liability for recalled products. The national-brand manufacturer bears all responsibility. By instituting a private label program, DeCA may be exposed to additional risks, liability and costs associated with any recalls of private label products.

Additionally, because DeCA is a name-brand benefit, strong relationships have been forged between manufacturers, DeCA and the patrons, whereby cause marketing and promotional programs have been implemented that have helped to raise millions of dollars each year to support organizations like the National Military Family Association, the USO, and Fisher House, among others, as well as numerous camp and college scholarships for military children. By instituting private label, DeCA will remove products from the shelf that support these efforts and reduce the amount of revenue generated through these cause marketing efforts. While the APF may be offset, military families get less quality-of-life support from their benefit.

In the end, if the costs are deemed to be bearable, we still believe that implementation should proceed slowly to ensure DeCA does not get saddled with too much product that it cannot move or on which it may take a loss. The Council recommends a test of a few private label products in a couple of categories to see how the patrons respond to both the loss of the national brand with which they are familiar, as well as the addition of a new untested, unfamiliar brand on the shelf.

In order for DeCA to institute private label and generate revenue from the products, variable pricing will be required. In other words, DeCA will have to abandon the cost-plus model. No matter which way it is communicated, the reality is we are asking military families to bear the burden of paying for the commissaries. We view this as breaking faith with our military families and sets a dangerous precedent.

While efforts in the short term may be to keep prices and savings the same, future DoD leaders in a non-transparent manner may require DeCA to raise prices further to garner additional revenue to

⁷ <http://www.vocativ.com/culture/health-culture/ice-cream-listeria-recalls-fda/>

offset APF. It presents a dangerous and slippery slope for commissaries. If Congress changes Title X to allow for variable pricing, the AFMC recommends that it be tightly constructed to protect patrons from future price increases that further diminish the benefit.

Price Rationalization

The AFMC is concerned with the concept of price rationalization. This suggestion calls for the equalization, or normalization, of savings across regions and across categories throughout the commissary system. Under this concept, patrons in some areas of the country, such as Hawaii, Alaska, Virginia, California, and high cost-of-living metropolitan areas, for instance, will see their prices increased while people in low cost-of-living areas will see their prices decrease.

This will result in winners and losers among patrons, but may likely be a lose-lose proposition for DeCA. DeCA runs the risk of losing patrons in areas where prices would be increased, which include the highest performing stores in the system, such as Pearl Harbor and Ft. Belvoir. This is a very real concern given BCG's analysis of patron price sensitivity as was discussed earlier.

We are also concerned with how price rationalization would impact cost of living adjustments (COLA) for families in adversely affected areas. We would hope that, since cost of living would be higher due to the price increases, that the COLAs would be adjusted accordingly. In turn, there would be no benefit to the patron or the taxpayer.

Price rationalization among categories would mean higher prices on meat, produce, and dairy products in order to lower prices on items in the center of the store. It puts DeCA at risk of losing patrons and patron loyalty due to higher prices on this essential categories of products meat, which serve to make a trip to the commissary worth the trip. While DeCA is not allowed to have loss leaders to attract patrons, meat, produce and dairy prices essentially serve that purpose for DeCA, attracting many patrons who drive miles to the commissary in order to stock up on items in those categories. And that also leads to additional foot traffic and sales in the exchanges.

Additionally, price rationalization will add another complex layer of operations and increased costs to manage and implement. Today DeCA is a simple model - sell products at cost plus. To

shift to price rationalization would require operational data systems and people with the proper skill sets to analyze the data and manage the program. That will result in additional operational costs which as of yet are undetermined.

Further, we believe price rationalization will likely produce a perception that the benefit is being eroded, particularly on categories of products important to patrons. And in the modern world of social media, it could have an adverse effect on DeCA's reputation as we are now seeing in the Pacific related to produce as patron perceptions become shaped more by the negative of higher prices on key categories rather than by the positive of lower prices on other categories.

We do not believe sufficient analysis has been conducted on price rationalization to determine the costs and whether any benefits would outweigh the costs or substantiate taking the risk. We do believe that any test of price rationalization should be limited and developed in such a way that it can be easily reversed if points of failure begin to emerge.

Converting DeCA to a Non-Appropriated Fund Instrumentality

The AFMC is cautiously supportive of this effort depending on the final plan. We are foremost concerned about the impact on the nearly 60% of DeCA's workforce that is made up of military family members and the impact job losses and/or wage reductions would have on their financial readiness.

We are also concerned with the upfront costs with conversion and the impact conversion would have in the short term on employee morale and the service levels provided to patrons. These are issues that certainly would need to be mitigated.

We support efforts to operate DeCA more efficiently and certainly personnel costs are a major cost center for DeCA. Evaluating and reviewing salaries to ensure they are commensurate with NAF wages is an important step in this effort. The AFMC also supports a staff structure review to determine whether requirements are adequately being met or if too many people are employed to fulfill the requirements. As was stated earlier, some stores are not manned to appropriate levels and we believe this is having an adverse impact on service to the patron.

But we also recognize that DeCA has long needed payroll flexibility to garner the best talent that is not currently resident with the organization to help achieve some its more complicated goals that require people with specific experience and new skill sets.

The AFMC is optimistic about the opportunity but concerned with the financial challenges related to implementation and the impact on service to the patron.

Local Sourcing

The concept of local sourcing is an attempt to reduce overseas shipping costs, otherwise known as Second Destination Transportation (SDT). Congress intentionally established SDT as a means to ensure military patrons around the world receive the same price that they would had they remained in CONUS. SDT funds ensured that military families stationed OCONUS were not penalized for serving overseas. The Council believes there is no better use of taxpayer dollars than ensuring that our military families in stationed in overseas are able to access at affordable prices quality-made, U.S. certified products.

Currently, we are watching closely the implementation of local sourcing of produce in the Pacific. While we recognize that a series of challenges and missteps led to \$10.69 bagged lettuce and other outrageous prices on other produce items in Guam⁸, we anticipate the prices will normalize as better shipping methods and better ordering systems are employed.

The current attempt in the Pacific requires first destination shipping to the stores instead of first destination to a distribution center then SDT funds used to pay for shipping to the store. This means that all shipping costs are included in the price of the product, which we believe violates the spirit and intent of Congress when it codified SDT into law.

⁸ <http://www.militarytimes.com/story/military/benefits/on-base/2015/12/20/some-pacific-commissary-produce-prices-spike-under-new-contracts/77501250/>

Discovering more efficient shipping methods to reduce SDT costs are encouraged, but so-called efficiencies that simply transfer shipping costs to patrons stationed at OCONUS bases are a violation of trust and legislative intent.

Another concern about local sourcing of products is the challenge of American military families knowing what they are buying. For instance, how does a military mom know if the product she seeks to purchase, that has a label in a language she can't read, will not trigger an allergic reaction in her child? How does she know what the ingredients are? As mentioned earlier in regards to private label products, how does that mom know whether the local government standards will protect her and her family from products that do not properly disclose ingredients?

SDT also has helped U.S. Transportation Command (TRANSCOM) maintain a high level of readiness during peacetime. If local sourcing is utilized, what will be the impact on TRANSCOM and its readiness?

Shelf stocking

The issue of shelf stocking in the commissaries has been a perennial discussion. Currently, manufacturers pay third-party contractors to stock commissary shelves with their products. It has been proposed that if DeCA takes on shelf-stocking, it could capture the monies being spent by manufacturers on stocking in the form of lower prices on products, take those monies and pay either government employees or contracted labor to stock the shelves.

First, the assumption that manufacturers would offer a lower price is false. The price DeCA receives from manufacturers is equal to the lowest price offered to any retailer per DeCA contract. The money used to pay stockers comes from other sources within their companies and is not reflected in the price of the product.

Additionally, the private vendor community is able to contract for shelf-stocking at a lower cost than DeCA currently does. Due to federal contracting rules, DeCA's costs will always be higher, that is, unless it is converted to a NAF. But even then, it must meet required minimum federal wage rates.

Regardless of DeCA's status, this would become a new cost center for DeCA with no assurances that the costs would be offset by revenues or lower product costs. Instead of becoming an efficiency, it would become another layer of cost added to DeCA's operations.

Again, we believe further full-spectrum analysis needs to be conducted that includes conversations with the vendor community to better understand how stocking is funded today and the impacts that would occur if DeCA assumes responsibility for shelf stocking.

MILSTAR in Commissaries

The AFMC supports allowing military patrons to use their MILSTAR card in the commissaries. We believe this is an opportunity to reduce overhead costs without having any adverse impacts on the patron, while also allowing the patron to reduce their credit card payments due to lower interest. However, if MILSTAR use is permitted in the commissaries, we believe an equitable distribution of revenue should be mandated.

Veterans Shopping Online Benefit

Historically, the AFMC has supported expanding privileges to categories of veterans, particularly those who are combat-wounded or have service connected disabilities.

The VSOB is an opportunity to offer an online benefit to all veterans which would not impact traffic in the stores nor would it adversely impact current patrons.

We see this as a great opportunity to increase sales, enhance the benefit for all patrons, and help to generate additional revenue to support the resale systems and MWR. We also believe that a fair and equitable portion of profits be shared with the Veterans Canteen Support in support of warrior care programs.

Advertising

Since DeCA was formed in the early 1990's, the world has changed. Unfortunately, DeCA was unable to change and adapt to keep the commissary benefit relevant to the patron.

The world is online and patrons can get the price of any product at most any store in a matter of seconds. The AFMC believes the commissary benefit can be greatly enhanced if DeCA were able to better communicate its offerings to its patrons. We encourage a relaxing of advertising restrictions on DeCA to allow it be more relevant to shoppers.

Online ordering and Pick-up

In line with outside-the-gate retailers, DeCA has successfully tested an online ordering system for patrons that allows them to submit an order to pick up on their way home from work. However, there are costs associated with fulfilling the orders that should be offset by a convenience fee.

The AFMC views online ordering as a worth-while enhancement of the commissary benefit. We support allowing DeCA to charge a convenience fee to support this program and allow it to be expanded throughout the commissary system.

Conclusion

While there have been numerous suggestions recommended to reduce DeCA's appropriation, the AFMC does not believe sufficient full-spectrum analysis has been conducted to determine the overall complexities and costs associated with implementing and maintaining the concepts.

The AFMC believes that before any reforms that change DeCA's operating model and/or seek to generate revenue from military families are tested or implemented, that full-spectrum analysis be conducted to fully understand the operational requirements and costs to implement. The analysis

should consider additional costs that may be required if the vendor community no longer provides the in-store ancillary support it currently provides.

Additionally, we believe that any reform efforts that are implemented are done so gradually and in such a way as they can be easily reversed if negative effects start to occur.

Lastly, for the good of our military families, the good of the commissary benefit, the good of the military exchanges, and the good of MWR programs, commissary reform should not aggravate the patron.

Thank you Chairman Heck, Ranking Member Davis and members of the Subcommittee for your kind attention.

Exhibit 1**Thomas T. Gordy
Curriculum Vitae**

Tom Gordy serves as the President of the Armed Forces Marketing Council, a position he has held since March 2008. In this role, he works to support and enhance the military resale benefit for military families by engaging with congressional and military resale industry leaders to address issues of concern to the members of the Council.

However, his work on military resale began in 2001 when he became personal staffer for a Member of Congress representing Virginia's Second Congressional District. The district included seven military bases and numerous resale and Morale, Welfare and Recreation programs.

Over the years, he has been involved in various issues related to military resale to include consolidation, commissary budget cuts, commissary efficiencies, interchange fees, product restrictions, base access for industry, tax issues, local sourcing, variable pricing, private label products, privatization, and more.

In 2007, Tom worked as a Senior Strategic Communications Consultant for The Wexford Group/ CACI supporting the congressional and public affairs directorates of the Joint Improvised Explosive Device Defeat Organization.

In November 2002, Tom was commissioned as a U.S. Navy Reserve Public Affairs Officer. From March 2009 to February 2010, Tom was mobilized to active duty and deployed to Iraq as the Legislative Affairs Officer and Deputy Public Affairs Officer to U.S. Army Gen. Ray Odierno, Commander, Multi-National Forces-Iraq. He is currently assigned to the Commander U.S. Naval Forces South/Commander Fourth Fleet reserve unit in Mayport, FL and is the officer in charge of the public affairs branch.

Since October 2008, Tom has successfully owned and managed River Woods Retreat, a mountainside log cabin vacation rental in Virginia's Shenandoah River Valley. And from 1989 to 1998, Tom served as youth minister, associate pastor and pastor in various churches in northeast Louisiana and Juneau, Alaska.

From 2013 to 2015, Tom served on the Board of Trustees of the Virginia Veteran Services Foundation, which provides funding for veterans services and programs in the Commonwealth through the Veteran Services Fund.

As a volunteer, Tom is the chairman of the Victory Elementary School Advisory Council, Bristow, VA, is an Elder and Director of Grace Life Community Church, Bristow, VA, and supports the Navy Safe Harbor Foundation, Alexandria, VA, which supports wounded, injured and seriously-ill Sailors and Coast Guardsmen.

Tom is a native of Monroe, LA and is a graduate of University of Louisiana at Monroe (BBA) and Regent University (MA).

Tom is married to the former Theresa Mayo of New Iberia, LA. They have two children and reside in Northern Virginia.

**DISCLOSURE FORM FOR WITNESSES
COMMITTEE ON ARMED SERVICES
U.S. HOUSE OF REPRESENTATIVES**

INSTRUCTION TO WITNESSES: Rule 11, clause 2(g)(5), of the Rules of the U.S. House of Representatives for the 114th Congress requires nongovernmental witnesses appearing before House committees to include in their written statements a curriculum vitae and a disclosure of the amount and source of any federal contracts or grants (including subcontracts and subgrants), or contracts or payments originating with a foreign government, received during the current and two previous calendar years either by the witness or by an entity represented by the witness and related to the subject matter of the hearing. This form is intended to assist witnesses appearing before the House Committee on Armed Services in complying with the House rule. Please note that a copy of these statements, with appropriate redactions to protect the witness's personal privacy (including home address and phone number) will be made publicly available in electronic form not later than one day after the witness's appearance before the committee. Witnesses may list additional grants, contracts, or payments on additional sheets, if necessary.

Witness name: Thomas T. Gordy

Capacity in which appearing: (check one)

Individual

Representative

If appearing in a representative capacity, name of the company, association or other entity being represented: Armed Forces Marketing Council

Federal Contract or Grant Information: If you or the entity you represent before the Committee on Armed Services has contracts (including subcontracts) or grants (including subgrants) with the federal government, please provide the following information:

2015

| Federal grant/ contract | Federal agency | Dollar value | Subject of contract or grant |
|----------------------------|----------------|--------------|---------------------------------|
| None | | | |
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2014

| Federal grant/ contract | Federal agency | Dollar value | Subject of contract or grant |
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Foreign Government Contract or Payment Information: If you or the entity you represent before the Committee on Armed Services has contracts or payments originating from a foreign government, please provide the following information:

2015

| Foreign contract/ payment | Foreign government | Dollar value | Subject of contract or payment |
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| None | | | |
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Statement

of the

NATIONAL MILITARY FAMILY ASSOCIATION

Before the

**Subcommittee on
Military Personnel**

of the

**UNITED STATES HOUSE OF REPRESENTATIVES
ARMED SERVICES COMMITTEE**

January 13, 2016

**Not for Publication Until Released by
The Committee**

The National Military Family Association (NMFA) is the leading nonprofit dedicated to serving the families who stand behind the uniform. Since 1969, NMFA has worked to strengthen and protect millions of families through its advocacy and programs. They provide spouse scholarships, camps for military kids, and retreats for families reconnecting after deployment and for the families of the wounded, ill, or injured. NMFA serves the families of the currently serving, retired, wounded or fallen members of the Army, Navy, Marine Corps, Air Force, Coast Guard, and Commissioned Corps of the USPHS and NOAA.

Association Volunteers in military communities worldwide provide a direct link between military families and the Association staff in the Nation's capital. These volunteers are our "eyes and ears," bringing shared local concerns to national attention.

The Association does not have or receive federal grants or contracts.

Our website is: www.MilitaryFamily.org.

Eileen Huck, Government Relations Deputy Director

Eileen Huck became Deputy Director in the Government Relations Department in October, 2012 after previously holding positions in the Youth Initiatives and Development Departments. In her role as Government Relations Deputy Director, Eileen monitors issues relevant to the quality of life of families of the Uniformed Services. Her areas of responsibility include military child care, children's education and Impact Aid; Commissary, Exchange and MWR; state initiatives, to include the Interstate Compact on Educational Opportunity for Military Children; and absentee voting rights. She also represents NMFA on the Military Coalition (TMC) Retired Affairs and Personnel, Compensation and Commissary committees and is chair of the TMC Awards Committee.

Prior to joining NMFA, Eileen volunteered as a case worker with the Navy-Marine Corps Relief Society in Mayport, Florida and served as adviser to the USS HALYBURTON Family Readiness Group. She earned Bachelor's and Master's degrees from Georgetown University and served two tours overseas as a Foreign Service officer. A Navy spouse, Eileen has lived in Virginia, California, Florida, and Rhode Island. She currently resides in Alexandria, Virginia with her husband, CAPT Michael Huck USN, and their two children.

Chairman Heck, Ranking Member Davis, and members of the Subcommittee, the National Military Family Association thanks you for this opportunity to provide testimony on the military resale system, a vital element of the total military compensation package. In recent years, the military resale system has come under increasing scrutiny as the Department of Defense, Congress, and the Military Compensation and Retirement Modernization Commission (MCRMC) have all put forward proposals to reduce commissary appropriations and streamline operations. Our Association understands and appreciates the need for efficiency and fiscal restraint. **However, we urge Congress not to reduce commissary funding or alter its operating structure without first carefully considering the impact on military families – particularly, the risk the savings they enjoy by shopping at the commissary will be reduced or lost.**

Military Families Value the Commissary

Our Association has always contended the value of the commissary is not just in the brick and mortar building on an installation; it is in the **savings** military families realize by shopping there. Research by the Defense Commissary Agency (DeCA) has shown families save an average of 30 percent when they shop at the commissary rather than at civilian grocery stores¹. We recognize the actual savings realized by individual families will vary based on their location and their buying habits. But, the fact remains the commissary's mandate to sell products at cost plus five percent provides service members with the reassurance they will be able to feed their families at a reasonable price wherever they're stationed. While this reassurance is important to all military families, it is especially vital to young families, those stationed in remote or high cost areas, and families living overseas.

Military families recognize the value of this benefit. In April 2015 we posted an article on our website describing some recent proposals regarding commissary funding and asked military families to share their views about the commissary benefit. We received dozens of responses from families eager to tell us how important the commissary savings are to their budgets and to their financial well-being:

"As a spouse at one of the remote locations (29 Palms) I can honestly say taking away or reducing our commissary benefit will impact our finances and food choices. While we have a smaller commissary it has all the basic things we need. It's already closed one day a week and that is hard enough. We didn't ask to be stationed here and punishing us by making us pay more for food to be brought here isn't fair."

"We are a family of six and have been in the military for seventeen years. The Commissary is something we have relied on at every duty station we have been. We are currently stationed in Alaska and use the Commissary and the Exchange on a weekly basis. With the prices in Alaska being higher than what we are used to, the comfort of the Commissary made it easier to make sure I have all I need to feed my family."

"As a military family recently moved from AZ to Southern CA, currently living on my husband's military income alone, the commissary is one of our saving graces. It's the only place we can

¹ DeCA News Release, "New Price Study Validates 30% Savings," January 9, 2014. www.commissaries.com

afford to shop and feed our family on our limited budget. If we are forced to shop at "in town" grocery stores, I'm not sure how we'll get by."

The challenges associated with military life only increase the importance of the commissary benefit. Due in part to frequent military-ordered moves, military spouses face much higher levels of unemployment than their civilian counterparts; research shows there is a 25 percent unemployment rate among military spouses. As a result, military families often find themselves relying on one income. Many of these young military families are eligible for nutrition assistance through the Women, Infants, and Children (WIC) program operated by the Department of Agriculture. For these families, commissary savings allow them to stretch their grocery budgets farther, helping ensure even the most junior service members can afford to feed their families.

In addition to providing savings to families, the commissary is also a major employer of military family members. Nearly two-thirds of commissary employees have a military affiliation². Any proposal to alter commissary operations must take into account the financial well-being of these employees and their families.

Shifting Costs Undercuts the Value of the Commissary Benefit

Reducing the commissaries' appropriation or altering its operations may not directly threaten the stores' physical existence. However, such proposals do risk undermining the value of the benefit by increasing prices and reducing the savings, either intentionally or unintentionally. The most extreme example is the provision included in the Administration's FY16 budget request that would have cut commissary appropriations by more than \$1 billion over three years. The Department suggested making up for the funding shortfall by increasing prices and transferring the cost of shipping goods overseas to commissary shoppers. Such price increases would present special hardship to junior military families and those in remote or overseas locations, who have few shopping options.

Clearly any plan that relies on increasing prices undercuts the value of the commissary benefit for military families. However, cutting the appropriation and relying on revenues to fund commissary operations would have other, unintended consequences, potentially threatening the existence of the system as whole. In 2015, DoD commissioned the RAND Corporation to conduct a study on the impact of price increases at the commissary. Unsurprisingly, the research showed if prices increase, families will shop elsewhere.³ In fact, RAND concluded price increases would actually lead to lower revenues for the commissary. Our conversations with military families consistently confirm RAND's conclusion. Many service members and families travel long distances and bypass more conveniently located stores in order to benefit from commissary savings. If commissary prices increase, it would no longer make sense for them to shop there:

² *Costs and Benefits of the Department of Defense Resale System*, Resale and MWR Center for Research, December 2012, pg. 4

³ *Bond, Craig, Julia Pollak, Bernard D. Rostker and Cate Yoon. The Likely Effects of Price Increases on Commissary Patronage: A Review of the Literature*. Santa Monica, CA: RAND Corporation, 2015. http://www.rand.org/pubs/research_reports/RR835.html.

"I would seriously reconsider shopping at the commissary if prices increased. This would negatively impact our junior enlisted families in particular."

"The reason I do shop there is because my overall bill is always cheaper compared to when I shop at other stores. I wouldn't shop there if they raised prices, there's no benefit to it."

Any proposal that envisions using commissary revenues to operate the system must consider what will happen if revenues decrease. We fear that faced with lower revenues DeCA would be forced to reduce operating hours, lay off employees, and ultimately close stores in order to cut operating costs. While DoD has expressed a commitment to preserving stores in isolated locations, we wonder at what cost? With lower revenues available to operate the system and yet with the continued need for stores in remote locations and overseas, how much savings will the Department actually realize? More importantly from our perspective, what would be the effect on families?

Allowing contractors to pass the cost of shipping goods overseas on to commissary shoppers places an unfair burden on families living overseas. Our Association has long contended there is a difference between benefits offered to service members and families and expenditures the Department must assume as a cost of doing business. For example, if the Department chooses to station families in remote locations it needs to provide programs and services to ensure those families can enjoy an adequate quality of life. Similarly, if the Department chooses to send service members overseas, it needs to ensure they are able to feed their families affordably. When lettuce costs more than \$10 a bag, as is now the case at commissaries in Guam and other Pacific locations following implementation of a new shipping contract⁴, the Department is failing to meet its obligations to military families. Forcing families to absorb the cost of shipping groceries overseas places an undue burden on families in those locations, who often have few other shopping options.

"In Hawaii, the commissary can be the reason a young family stays solvent. Yes, they get COLA, but at \$7 a gallon for milk, \$35 for a container of formula, that COLA disappears fast."

Finally, it is also important to consider the effect cuts to commissary funding would have on the Exchange system. Although they both serve military families and operate on military installations, the commissaries and Exchanges have completely different mandates and business models. The Exchanges are non-appropriated fund activities and fund most of their operations from profits on the items they sell. Any revenue that exceeds operating cost is used to fund installation Morale, Welfare and Recreation (MWR) programs. The Exchanges are highly reliant on traffic from the commissaries. If increased commissary prices lead military families to shop elsewhere, it is reasonable to assume Exchange sales will drop as well. What will that lost revenue mean for installation MWR programs, which are highly valued by military families?

Consolidation and Privatization: How Would Plans Affect Military Families?

In its January 2015 report, the Military Compensation and Retirement Modernization Commission (MCRMC) recommended consolidating commissaries and Exchanges in a single defense retail operation. While we appreciate the Commission's recognition of the importance of commissary

⁴ "Some Pacific commissary produce prices spike under new contracts," Military Times, December 20, 2015

savings and their efforts to preserve the benefit, we have concerns about the cost and consequences of consolidation. As noted above, the missions and operating structures of the two systems are quite distinct; in addition, the Exchange itself is actually comprised of three different systems operated by the Service branches. Previous attempts to consolidate the Exchange systems have failed due to logistical complications and Service objections. We are skeptical it is possible to combine the systems in a way that would maximize efficiency while still preserving the savings for military families. And again, we have to ask what would happen if insufficient revenues are generated to support a consolidated system? Our skepticism about the viability of consolidating the entire DoD resale system into one entity is justified, we believe, because of the history of failed efforts to consolidate the three Exchange systems.

Other proposals in recent years have suggested reducing the commissary appropriation by privatizing its operations. We note the MCRMC reported it investigated this option and concluded that no private entity would be willing to take on commissary operations while committing to preserve the savings. We agree with the Commission that privatizing the commissary runs the risk families will face higher prices and/or reduced operations as a private entity seeks to maximize revenue.

The FY16 NDAA authorized DoD to establish pilot programs that would evaluate the feasibility of various changes to commissary operations, including privatizing part or all of the system. We thank Congress for its emphasis on preserving savings for military families in this provision. However, the military resale system is highly interdependent; changes to one element of the system may have unintended consequences that will affect other parts. For example, if one or more high volume store is privatized will DeCA still benefit from economies of scale that allow vendors to sell goods at low cost? What would removing those high volume stores from the system mean for smaller stores or those in remote locations?

Most Recent DoD Proposal Raises Questions

In December, 2015 the Department released a fact sheet outlining its plans to “optimize” the Defense resale system. We are gratified the Department acknowledges the importance of the commissary benefit and states its commitment to preserving the value of the benefit for military families. However, we have concerns about how the Department’s plans will be put into practice and how military families will be affected by efforts to optimize commissary operations. Specifically, we ask Congress to require DoD to provide answers to the following questions:

- *Definition of “tangible and intangible” benefits.* How does the Department intend to measure the benefits of the commissary system as currently constructed, and what metrics will it use to ensure any changes do not lead to a reduction in those benefits?
- *Composition of Defense Resale Business Optimization Board.* Does the Department intend to seek out stakeholder views before implementing any changes recommended by the Board?
- *Plans for “pricing flexibility.”* As noted above, changing the traditional “cost plus five percent” pricing system has already negatively impacted families living in Guam. How will the Department implement price flexibility while ensuring families continue to receive the full value of the commissary benefit?

In short, we are asking the Department for **transparency in its decision-making process**. Military families need and deserve the assurance their well-being is prioritized before any aspect of commissary operations is changed.

We acknowledge it is difficult to accurately assess the value of the commissary to the military community as a whole without detailed information about who is using the commissary and what they choose to purchase. Through our conversations with military families we know many of them highly value the commissary benefit; the MCRMC came to the same conclusion. However, there is little readily-available data detailing for example whether patrons are predominantly young families, more senior personnel, or retirees. Ironically, we know DeCA has this information as every shopper has to scan his or her ID card when making a purchase. We ask Congress to require DoD to release data on commissary shoppers so military families have the reassurance any changes to the system help those who most rely on the benefit.

In closing, we note that maximizing revenue has never been a priority for the commissary – nor should it be. The mission of the commissary is to provide military families with a vital non-pay benefit: the savings they realize by shopping there. While it is always possible to find efficiencies, we would argue DeCA has fulfilled its essential mission effectively and well. **We ask before making any changes to the commissary's operations, Congress first consider the impact on military families, many of whom rely on commissary savings to help ensure they are ready and able to support their service member.**

Eileen Amer Huck
Deputy Director, Government Relations
National Military Family Association

Eileen Huck became Deputy Director in the Government Relations Department in October, 2012 after previously holding positions in the Youth Initiatives and Development Departments. In her role as Government Relations Deputy Director, Eileen monitors issues relevant to the quality of life of families of the uniformed services. Her areas of responsibility include Military Child Care, Children's Education and Impact Aid; Commissary, Exchange and MWR; State Initiatives, to include the Interstate Compact on Educational Opportunity for Military Children; and Absentee Voting Rights. She also represents the Association on the Military Coalition (TMC) Retired Affairs and Personnel, Compensation and Commissary committees and is chair of the TMC Awards Committee.

Prior to joining the Association, Eileen volunteered as a case worker with the Navy-Marine Corps Relief Society in Mayport, Florida and served as adviser to the USS HALYBURTON Family Readiness Group. She earned Bachelor's and Master's degrees from Georgetown University and served two tours overseas as a Foreign Service officer. A Navy spouse, Eileen has lived in Virginia, California, Florida, and Rhode Island. She currently resides in Alexandria, Virginia with her husband, CAPT Michael Huck USN, and their two children.

About the National Military Family Association: Military families serve our country with pride, honor, and quiet dedication. The National Military Family Association is the leading nonprofit organization committed to strengthening and protecting the families of the men and women currently serving, retired, wounded or fallen. We provide families of the Army, Navy, Marine Corps, Air Force, Coast Guard, and Commissioned Corps of the USPHS and NOAA with information, work to get them the benefits they deserve, and offer programs that improve their lives. Our more than 40 years of service and accomplishments have made us a trusted resource for military families and the Nation's leaders. To learn more, visit www.MilitaryFamily.org.

**DISCLOSURE FORM FOR WITNESSES
COMMITTEE ON ARMED SERVICES
U.S. HOUSE OF REPRESENTATIVES**

INSTRUCTION TO WITNESSES: Rule 11, clause 2(g)(5), of the Rules of the U.S. House of Representatives for the 114th Congress requires nongovernmental witnesses appearing before House committees to include in their written statements a curriculum vitae and a disclosure of the amount and source of any federal contracts or grants (including subcontracts and subgrants), or contracts or payments originating with a foreign government, received during the current and two previous calendar years either by the witness or by an entity represented by the witness and related to the subject matter of the hearing. This form is intended to assist witnesses appearing before the House Committee on Armed Services in complying with the House rule. Please note that a copy of these statements, with appropriate redactions to protect the witness's personal privacy (including home address and phone number) will be made publicly available in electronic form not later than one day after the witness's appearance before the committee. Witnesses may list additional grants, contracts, or payments on additional sheets, if necessary.

Witness name: Eileen Huck

Capacity in which appearing: (check one)

Individual

Representative

If appearing in a representative capacity, name of the company, association or other entity being represented: National Military Family Association

Federal Contract or Grant Information: If you or the entity you represent before the Committee on Armed Services has contracts (including subcontracts) or grants (including subgrants) with the federal government, please provide the following information:

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T H E M I L I T A R Y C O A L I T I O N

201 North Washington Street
Alexandria, Virginia 22314
(703) 838-8143

STATEMENT FOR THE RECORD
OF
THE MILITARY COALITION (TMC)
Submitted to the
HOUSE ARMED SERVICES
SUBCOMMITTEE ON MILITARY PERSONNEL
concerning
Views on Commissary Reform
January 13, 2016

Chairman Heck, Ranking Member Davis, and distinguished members of the Subcommittee, on behalf of The Military Coalition (TMC), a consortium of nationally prominent uniformed services and veterans' organizations, we are grateful to the committee for this opportunity to express our views concerning commissary reform. This statement for the record provides the collective views of the following military and veterans' organizations, which represent approximately 5 million current and former members of the seven uniformed services, plus their families and survivors.

Air Force Sergeants Association
 Air Force Women Officers Associated
 AMVETS
 Army Aviation Association of America
 Association of Military Surgeons of the United States
 Association of the United States Army
 Association of the United States Navy
 Chief Warrant Officer and Warrant Officer Association, U.S. Coast Guard
 Commissioned Officers Association of the U.S. Public Health Service, Inc.
 Enlisted Association of the National Guard
 Fleet Reserve Association
 Gold Star Wives, Inc.
 Jewish War Veterans of the United States of America
 Marine Corps Reserve Association
 Military Chaplains Association of the United States of America
 Military Officers Association of America
 Military Order of the Purple Heart
 National Association for Uniformed Services
 National Guard Association of the United States
 National Military Family Association
 Naval Enlisted Reserve Association
 Non Commissioned Officers Association
 Reserve Officers Association
 The Retired Enlisted Association
 United States Army Warrant Officers Association
 United States Coast Guard Chief Petty Officers Association
 Veterans of Foreign Wars

The Military Coalition, Inc. does not receive any grants or contracts from the federal government.

First and foremost, we express our deep thanks to this Subcommittee for your longstanding support of the commissary program and your commitment to maintaining the value of this important benefit for the entire uniformed services community. It is solely because of your strong support that the commissary benefit has been preserved from those who, over the course of many decades, have sought to weaken, defund, privatize, or eliminate it entirely.

Last year's Administration proposal to phase out the commissary subsidy over several years was only the latest of these efforts. It focused entirely on cutting spending, with little regard for the dramatic reduction in compensation value such action would impose on millions of currently serving, retired, and survivor patrons and family members.

This committee's insistence on preserving the current levels of patron savings, satisfaction and high product quality – and specifying those requirements in the FY2016 National Defense Authorization Act (NDAA) – has been crucial to altering the tone and direction of the discussion on commissary changes. Your specification of these standards of measurement for any effort to make commissaries cost-neutral effectively forced the Defense Department (DoD) to acknowledge the reality that the two are mutually exclusive. That is, any major reduction in funding must necessarily lead to reduced patron savings, satisfaction, and product quality.

We are deeply gratified that DoD's Deputy Chief Management Officer (DCMO) Peter Levine acknowledged that past proposals focused on cost-cutting over maintaining the benefit. He has assured us that, thanks specifically to your efforts, savings to the patron is now the Department's priority, and cost cutting will only be implemented to the point that patron savings are sustainable at current benchmark levels. In that vein, the Coalition believes any proposed changes to commissary programs must be evaluated against these same NDAA-established standards – i.e., would the proposal sustain patron savings and satisfaction?

Why Commissaries Exist

For nearly 200 years, our government has funded commissaries, in one form or another, for our military personnel. The original purpose was to provide goods on post without involving civilian vendors, to allow the Army to care for its own by providing more than was available through rations, and to supplement military pay.

As the government began assigning servicemembers to remote and overseas locations, commissaries evolved to provide members, and then families, relief from limited food options in the remote or overseas locations, and to sustain access to the kinds of food and other products they would have had available if the government had not assigned them to such locations. Finally, acknowledging the particular compensation value of the commissary program, an additional purpose has been to provide a reasonably consistent benefit across the range of locations where substantial numbers of servicemembers and families are assigned. Military personnel can rely on finding a similar offering of items at military installations around the world.

As military demographics have changed over the decades, to include more and more families, military personnel policy also has evolved to recognize the retention value of family-related programs, including not just commissaries, but healthcare, housing, funding for local schools, family programs, and more that reflect the needs of military families and their effect on military readiness.

The Commissary Subsidy Is Cost-Effective

The commissary remains one of the most cost efficient benefits provided by the DoD to our military families, in terms of benefit value delivered per federal dollar spent. If an E-5 (8 years) with a family of four spends \$600 per month at the commissary that provides a savings level of 30%, those same items would cost \$857 in a civilian store. The difference of \$257 per month is a direct compensation value for that enlisted family. In effect, that level of monthly savings is equivalent to a 9% basic pay raise compared to what the family would spend on food if the commissary were removed from the equation.

For the last three years, military families have seen pay raises smaller than in the private sector, cutbacks to housing allowances, increases in pharmacy copays, and increasing numbers of pink slips given. Military families are not providing fewer sacrifices in their service to our nation. But they are being asked to do so with fewer dollars, fewer support programs, and fewer training opportunities.

In the midst of all these cutbacks, the commissary continues to provide a substantial, consistent and highly valued compensation offset. Study after study has shown commissaries rank only behind healthcare as the most valued non-cash benefit, and that significant commissary cuts would reduce morale and pose a threat to retention.

Reports and Recommendations to Consolidate

The Military Compensation and Retirement Modernization Commission (MCRMC) proposed to consolidate the broader military resale system, merging commissaries and Exchanges. The Military Resale Study by Boston Consulting Group (BCG) and the proposals outlined by the DoD would consolidate backroom and high level administrative activities only. While the 1990's merge of separate commissary agencies into Defense Commissary Agency (DeCA) was successful, efforts to merge the separate Exchanges have not been, in part because of different service structures.

The laws that define what the commissary and Exchange can each sell allow them to provide savings benefits to the same servicemember without competing directly. In fact, studies have shown patronage at one results in increased foot traffic and sales for the other. The performance of the two entities has been carefully integrated into the support activity structure on installations around the world.

The Exchanges are able to subsidize numerous activities on installations and during contingency operations with their profits. These include lodging, MWR activities and quality of life programs, varying by service and location. Any changes to the way the two interact or perform their current missions inevitably raise the potential for adverse effects on other smaller programs funded via MWR dividends. A RAND review confirmed these potential deficits and other secondary effects resulting in higher costs for the DoD to adequately support military personnel.¹

We urge caution in pursuing legislative changes to that nexus with secondary and tertiary effects on other quality of life programs. MWR programs remain vital to the support of servicemembers and their families, and their cuts have the potential to affect retention. While retention is not a driving concern during times of downsizing, the potential effects over the long term must be evaluated.

While many consolidation issues may be considered strictly "business decisions," the NDAA-imposed standards should still be the primary measuring stick. Would the proposals sustain or erode the current levels of patron savings, benefits, and satisfaction?

¹ The Likely Effects of Price Increases on Commissary Patronage, RAND, (2015).

Changes to Merchandising, Private Label and Surcharge Rules

The BCG report made several recommendations that would require legislative action. We believe it is reasonable to provide DeCA more operational flexibility in the way it provides service, so long as patron savings and satisfaction are maintained. These changes could include flexibility in merchandising, the use of a private label and how the 5% surcharge is used. Many times, DeCA has been asked to find efficiencies, only to respond they have cut all of the “low hanging fruit.” We believe them.

We are not fully convinced that these changes are the golden ticket to generating savings while preserving the benefit. We have questions about how these changes will provide customer satisfaction and high product quality.

Currently, customers get name brand items for low prices. It is unclear how a change in the variety of name brand items to a different ratio of private label items might affect customer satisfaction, savings or product quality. The RAND report cites that commissaries have a significantly smaller footprint than most private grocery stores and already sell a smaller selection of items.² Private grocers’ flexibility in pricing on the private label items allows them a larger profit margin, while DeCA has a mandate to provide savings.³ These are two very different goals. Additionally, DeCA would need to “add team members to manage relationships with third-party private label manufacturers or sourcing companies.”⁴ This proposal is not a simple one, with potential wins and pitfalls.

Additionally, we have seen commissary sales fall over the last several years. Some may attribute this to downsizing, but others might cite the possibility of lower customer satisfaction. Budget cuts have resulted in reduced hours, and perceived degradation in store performance or appearance reduces patronage. It is important to look at each commissary and determine whether it has what it needs to “sell” the products. Is it clean? Are the shelves fully stocked? Does it look inviting? Are the aisles wide enough for a cart full of children and a wheelchair to get by one another? Does security, parking, or other barriers make it too difficult to use the benefit? Flexibility to preserve savings may be useless if funding is cut in other ways that make commissaries less desirable and accessible.

The bottom line is the Coalition is not opposed to pursuing additional flexibility for DeCA managers to find additional savings options, but the net effect of any such flexibility adjustments must be scrutinized for potential impact on the patron experience.

Conversion to NAF system

We have some concern about other proposals requiring legislative action that will have a potential employee impact. Many of DeCA’s employees are military affiliated, meaning they are military family members or veterans/retirees themselves. In 2012, approximately 27% of DeCA’s 15,276 employees were military spouses or family members.⁵ BCG proposes that savings can be achieved in store operations by reducing dependence on contract labor and increasing the number of employees, but with all under a Non-Appropriated Fund (NAF) system. This includes converting current employees under the General Schedule (GS) system to NAF positions. Such a conversion includes a significant cut in wages and benefits for these employees.

²The Likely Effects of Price Increases on Commissary Patronage, RAND, pg. 18, (2015).

³Military Resale Study, Boston Consulting Group, pg. 42 (July 10, 2015).

⁴Id., pg. 44.

⁵*Costs and Benefits of the Department of Defense Resale System*, Resale and MWR Center for Research, pg. 32 (December 2012).

We understand this conversion will result in congruency for business and IT systems necessary to achieve savings. It is our hope that plans going forward will include equivalent substitute compensation packages for employees being converted to NAF status and that retirement and other benefits already earned will be "cashed out" for deposit in the new system. Where possible, we would urge that such changes be done through natural attrition.

Locally Sourcing Food, Elimination of Second Destination Transportation Subsidy

The BCG study identifies potential changes that can be implemented without legislation. One of these is locally sourcing goods, thereby reducing or eliminating the second destination transportation (SDT) subsidy for getting foods to overseas locations.

In 2014, DeCA proposed a larger portion of their produce in Pacific commissaries be sourced locally for savings. Some advocates, industry experts, and legislators, including members of this subcommittee, were concerned the change would result in lower quality and more expensive produce for patrons in those OCONUS locations.

DeCA has been able to do this in Europe fairly successfully, as the type of produce available there is more in common with that in the United States. This is not so easily achieved in Asia, where produce availability is highly variable. As such, implementation has not gone as smoothly as hoped. In Asia, where produce must be transported across oceans, the higher costs for procurement and transportation have been passed onto the patron. In December, a Military Times article outlined some of the difficulties, highlighting that the price for a 22-ounce package of Romaine lettuce in Guam had increased to \$10.69.

The Coalition believes strongly the SDT subsidy is a cost of doing military business, as the whole reason military members and families are assigned overseas is for military readiness. Therefore, we believe the SDT subsidy should be borne by the taxpayer through appropriated funding; ensuring our servicemembers and their families can eat healthy fresh food they are familiar with. Removing the subsidy results in it being figured into the cost borne by the contractor, and passed on to the patron. Servicemembers and their families are overseas at the pleasure of their government. They should not be responsible for paying for the cost of transporting necessary support goods to that location.

This subcommittee has been highly supportive of retaining the SDT, and we thank you for it, and ask that you continue to fight its elimination. The SDT is necessary to provide high product quality, sustain savings and maintain customer satisfaction.

Store Hours

DeCA has had to resort to cutting hours or days of operation as appropriations have been reduced. This has damaged patronage and customer satisfaction. Our military requires a lot from our servicemembers and their families, and requires it at all hours, whether it is convenient to the family schedule or not. However, many of the support functions have limited hours in comparison. Additionally, store hours being available after work on weekends is especially important to Guard and Reserve members who may only have access to commissaries during drill weekends.

We know that military families value access to the commissary. When hours of operation are limited, it impacts a family's access to the benefits required. This forces them to choose more convenient, albeit more costly options to provide for their family needs when the commissary isn't available. We oppose

cutting hours of operation as a cost saving measure because it does not meet the benchmarks of preserving savings and customer satisfaction.

Market Basket Savings Standard

One concern we have is possible changes to the calculation of savings based on a newly defined market basket. DeCA calculates their average savings of 30% on an annual market basket study of the pricing of thousands of items compared against other grocery stores, regionally.⁶ However, the BCG study used a different market basket analysis using 50 key items compared locally, and calculated that the average savings was only 16-21%.⁷ A new market basket benchmark could potentially reduce savings to patrons if limited compared to DeCA's broad measure. We ask that DeCA's annual market basket methodology be retained to ensure savings levels are measured accurately against the current savings benefit.

Conclusion

The Coalition is grateful to the Subcommittee for this opportunity to present our views. We are particularly grateful for your leadership in establishing patron-based benchmarks against which proposals can be measured. This is the most significant development on commissary issues in many years. Any changes that undermine DeCA's ability to attract a stable patron base effectively erode the benefit. Changes in pricing formats, funding for store maintenance and improvements, and funding for new marketing strategies all have the potential to impact patronage for the better. On the other hand, such changes have at least some potential for adverse consequences. While savings and satisfaction can be measured in surveys, declining patronage is also a concern that must be monitored as an additional indication of declining patron satisfaction.

It must be emphasized that a decrease in commissary usage does not just mean a reduction in surcharge revenue. It brings a reduction in Exchange foot traffic (i.e. shoppers and their profits) and reduced MWR dividends. Those reduced dividends mean that important quality of life and MWR programs lose their primary source of funding as a Non-Appropriated Fund activity. This threatens readiness, morale and retention.

The commissary is not just a DoD-operated grocery store. It is not a failing business model. In fact, it is not a business at all. It is a landmark benefit provided by DoD as part of the cost of doing business and supporting an all-volunteer-force. It provides food and goods to servicemembers stationed in remote locations with few shopping choices, and an opportunity to connect with their military community in high density areas. For those stationed overseas, it allows them to recognize the food that they buy, be able to afford it, interact with store employees in a language they understand, and experience a little taste of home to ease some of the challenges of military life. It gives access to the retiree to help make ends meet and an opportunity to maintain a connection to their military community. It is also important to families who are straining to make ends meet financially, providing them with more goods for their dollar than they can get elsewhere.

The commissary remains a landmark benefit common to generations of servicemembers. It is tremendously efficient for the cost of maintaining it, putting real compensation value in the pocket of every servicemember, retiree and wounded warrior who uses it far exceeding the amount of federal

⁶ New Price Study Validates Commissary's 30% Savings, http://www.commissaries.com/press_room/press_release/2014/DeCA_01_14.cfm (accessed Jan. 5, 2016).

⁷ Military Resale Study, Boston Consulting Group, pg. 26 (July 2015).

outlays for the commissary subsidy. That value can't be replaced, and if broken, may not be easily repaired.

Thank you again for your continued strong support of the commissary and the millions of patrons who use them.

Brooke Goldberg

Deputy Director, Government Relations (Military Family Issues)
Military Officers Association of America

Mrs. Brooke Goldberg is a graduate of the University of Oregon, with a Bachelor of Science in Political Science, a Minor in Spanish, and a Juris Doctorate with certificates in Environmental and Natural Resource Law and International Law. Goldberg is also eligible for a Professional Teaching Certificate in English as a Second Language. Goldberg has been an Air Force spouse since 2002, serving as a Key Spouse at both the installation and headquarters levels during her family's time assigned to Hurlburt Field, Florida. She has served as the Secretary and Vice President of the Board of Directors for a non-profit with an annual budget of \$2 million dollars, and taught Spanish for two years in Santa Rosa County public high schools.

She is now an Air Force Reserve Key Spouse serving at the Wing level at Dover Air Force Base, Delaware. She has served on the DoD Financial Readiness Roundtable, the Military Saves Advisory Roundtable, and several subcommittees of The Military Coalition (TMC). She currently sits on the Personnel, Compensation and Commissary and Military Construction/MWR subcommittees of TMC and the Department of Defense Military Spouse Ambassador Network.

Goldberg joined MOAA in 2015 after serving two years as Deputy Director of Government Relations at the National Military Family Association.

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Witness name: Brooke Goldberg

Capacity in which appearing: (check one)

Individual

Representative

If appearing in a representative capacity, name of the company, association or other entity being represented: Military Officers Association of America

Federal Contract or Grant Information: If you or the entity you represent before the Committee on Armed Services has contracts (including subcontracts) or grants (including subgrants) with the federal government, please provide the following information:

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DOCUMENTS SUBMITTED FOR THE RECORD

JANUARY 13, 2016

TESTIMONY OF

AMERICAN FEDERATION OF GOVERNMENT EMPLOYEES, AFL-CIO

**BEFORE HOUSE ARMED SERVICES SUBCOMMITTEE ON
MILITARY PERSONNEL**

ON COMMISARY REFORM

JANUARY 13, 2016

The American Federation of Government Employees (AFGE), AFL-CIO, which represents more than 650,000 federal employees in almost 70 different agencies who serve the American people across the nation and around the world, including in the Defense Commissary Agency (DeCA), is submitting testimony for the record for today's hearing. As the representative of a significant stakeholder, AFGE regrets that it was not given an opportunity to present the views of DeCA's workforce at the hearing.

AFGE is proud to represent civilian employees who work for DeCA, which provides groceries and household goods through more than 250 commissaries to active-duty, Guard, Reserve, and retired members of all seven uniformed services of the United States as well as eligible members of their families.

Authorized customers buy items at cost plus a 5% surcharge, which covers the costs of building new commissaries and modernizing existing ones. Shoppers save an average of more than 30 percent on their purchases compared to commercial prices—savings that amount to thousands of dollars annually when shopping regularly at commissaries.

It has been reported that the commissaries provided military households with \$2.7 billion in price savings and another \$200 million in income for military family members employed by DeCA; 90% of active-duty military families used the commissaries in 2012, helping to rack up 100 million customer transactions at DeCA annually. As a core military family support element, and a valued part of military pay and benefits—according to surveys of military personnel—commissaries enhance the quality of life for America's military and their families, and help to recruit and retain the best and brightest men and women to serve our country.

Thanks to Senators Jim Inhofe (R-OK) and Barbara Mikulski (D-MD), the Senate's FY16 NDAA was stripped of a provision that would have led to the privatization of the commissaries. However, having saved the commissaries from abolition and privatization, now the commissaries face a new threat—loss of almost all appropriations funds and conversion of DeCA to a non-appropriations funded (NAF) agency, which would have severe consequences for the agency's workforce and the long-term viability of the commissary benefit.

The FY16 NDAA included a provision that requires the Department to report how it would provide the commissary benefit as revenue neutral. In other words, the substantial benefit that DeCA provides to military families would somehow have to pay for itself—with no subsidies. DoD had earlier hired a business consultant, the Boston Consulting Group (BCG), to provide recommendations for how to take DeCA "off budget".

The three most important recommendations made by BCG are to

1. Introduce private labels, which many retail experts say is not feasible because DeCA's sales are not significant enough;

2. Use variable pricing, which is code for increase prices, and which many fear will drive away military families and lead to the end of the commissaries; and
3. Convert DeCA from appropriations fund status to NAF status, which would have a severely adverse impact on the workforce.

With respect to the third recommendation, conversion to NAF status would cut the pay of DeCA workers by as much as one-quarter, force them to pay significantly more for health care insurance, render them ineligible for retirement benefits, and make it easier to fire them and privatize their jobs. Here are relevant excerpts from BCG's report:

"The primary cost-saving benefit of NAF conversion for DeCA would be tangible reduction in labor costs...the NAF environment tends to provide for lower and more flexible wage schedules compared to APF. We estimate that annual run-rate savings in wages and benefits combined could be \$95-155M."

"Our analysis suggests that NAF conversion could enable 15-25% wage savings for in-store positions, while maintaining the same level of pay for above-store positions. Beyond differences in pay, there are also potential cost savings from benefits."

"Furthermore, DeCA would become more agile in terms of personnel actions. DeCA would be able to more speedily hire and separate employees, use business-based actions to adjust the size of the workforce, increase the use of flexible employees who do not receive benefits..."

"DeCA's share of full-time store level employees is greater than what we see in private sector grocers. Today, 63% of DeCA's in-store employees are part-time, which is 7-12% less than the 70-75% range we typically see in the private sector. Furthermore, all DeCA employees receive pro-rated benefits, even when working fewer than 30 hours per week. By shifting the labor mix towards industry levels and shifting some part-time employees to a flexible, non-benefitted status, DeCA could reduce store labor costs by \$10-25M."

"DoD instructions that govern NAFs constrain employers significantly less in defining employment terms than OPM regulations which cover APF entities. Major categories of differences include reduction and realignment, employee relations, and staffing. First, NAFs are able to use Business Based Actions (BBA) to reduce force, which use more flexible criteria than Reduction in Force (RIF) procedures that APF entities must follow. For example, whereas RIFs are restricted to specific purposes such as reorganization, lack of funds, and elimination of duties, BBA procedures can be used for a wider range of reasons including business realignments and a need to be competitive with the local labor market. Moreover, NAFs have greater flexibility in determining which employees

to separate because the primary factor in the BBA selection process is performance, whereas the APF RIF process is seniority-focused. Additionally, APF employees tend to have more formal recourse for grievances and appeals. For example, they are able to appeal adverse actions to the Merit Systems Protection Board (MSPB), and APF employers have the burden of proving that their actions were justified. In contrast, NAF employees only have the right to appeal to MSPB for issues concerning retirement portability and specific violations of their employment rights."

Various rationales will be offered to justify robbing the employees to keep the commissaries running:

"If we don't do this, they will privatize the system or get rid of the commissaries." However, stripping the commissaries of their subsidies makes it more likely that prices will have to be increased—which will drive off customers and lead to DeCA's demise.

"Commissaries are losing money on every sale—we have no choice!" Commissaries provide a substantial benefit to military families, one which just about everybody acknowledges is vital to personnel retention and the creation of military culture, so why shouldn't taxpayers pay for it? Such subsidies certainly better support the Department's mission than the billions upon billions of taxpayer dollars wasted annually on bad service contracts.

"Somebody has to sacrifice to keep the commissaries running, so why not the employees?" No DeCA employee is living large on her modest paycheck. In fact, many DeCA employees are veterans and military spouses whose families depend on their jobs.

"Well, maybe the cuts will only apply to future workforces, and we can grandfather current employees. But let's remember, DeCA employees earn more than their counterparts in the exchanges and the private sector." Why should the Congress arbitrarily pay workers significantly less for doing the same work? Why should the Congress engage in beggar-thy-neighbor economics and race-to-the-bottom politics? Why shouldn't the Congress be building up the middle class, as opposed to tearing it down?

A senior DoD official has already acknowledged that it would be "impossible" for the commissary benefit to continue to be meaningful for military families if DeCA were required to be revenue neutral, and that appropriations for the agency would continue to be necessary. The question is: how much funding will DeCA continue to receive?

DeCA should continue to strive to achieve efficiencies in the provision of the commissary benefit. However, there is no shame in taxpayers continuing to subsidize this important earned benefit, as just about anything of real value must ultimately be paid for. And although the commissaries have attracted extraordinary attention from policymakers in the legislative and

executive branches, it must also be acknowledged that DeCA's \$1.4 billion appropriation is a tiny fraction of the Department's budget.

Lawmakers should reject proposals to use the FY17 National Defense Authorization Act (NDAA) to reduce the cost for the provision of the commissary benefit through the imposition of extraordinary sacrifices on DeCA's already modestly compensated workers, many of whom are veterans and military spouses. Given the undeniable and substantial benefit provided to military families by the commissary benefit, it is imperative that we proceed carefully with proposals such as the introduction of a private label, use of variable pricing, and conversion of DeCA to non-appropriations funded status. The FY16 NDAA provided the Department with pilot project authority, and it makes sense to use that authority before attempting to implement major reforms.

QUESTIONS SUBMITTED BY MEMBERS POST HEARING

JANUARY 13, 2016

QUESTIONS SUBMITTED BY MR. JONES

Mr. JONES. Military compensation continues to receive considerable scrutiny. What are the major concerns identified by your constituents over commissary reforms?

Mr. NIXON. While DOD has said that they don't want to reduce the commissary benefit, the principle concern is that management savings initiatives will prove illusory and cuts will have to be absorbed by the patrons in the form of higher prices or reduced quality. For example, the fiscal year 2017 budget proposal reduced commissary funding by \$221 million. Were Congress to accept this reduction, we are concerned that reform and efficiency initiatives will fall short and leave the patron holding the bag. Second, there continues to be active talk of privatization of the stores. Our concern here is that it will be either tested or mandated system-wide. Privatization carries major risks for patrons and the Government. If it fails, you won't be able to reconstruct the system. We are also concerned about predictability for patrons. Commissary patrons are accustomed to high levels of savings and high quality. The efforts by the DOD to institute more generic brands and experiment with price variations either by region or commodity may weaken the patrons' confidence in the benefit. And, success or impact of these pilot programs needs to be measured against a solid verified baseline and quickly reversed if there is a negative impact on the benefit. As patrons lose confidence, they will migrate. The system will lose economies of scale and that will result in price spirals and sacrifices in quality. Elaboration on these concerns and other concerns with these reforms are presented in our prepared testimony.

Mr. JONES. What measurements should be imposed to determine if commissary reforms are beneficial or harmful to the commissary benefit?

Mr. NIXON. We need to ensure that solid, understandable and sensible metrics are put in place that gauge the impact to patrons. The commissary agency already has in place a solid, time-tested method of measuring savings to patrons and other benefits to the Government from commissary programs. This should be verified and used as the baseline to which alternative pricing models are measured. There needs to be careful analysis against this baseline before any pricing variation pilots are implemented. As any pilot programs are implemented, the impact needs to be measured against this baseline.

Mr. JONES. Recognizing that there continue to be supporters of the privatization commissaries and zeroing out the appropriated funding, how would you propose to reduce the appropriated cost of commissaries?

Mr. NIXON. Commissary appropriations already have dropped 40 percent or \$600 million per year in real terms from when the Defense Commissary Agency was founded in 1991. 180 of the 420 stores that existed in 1991 have closed. Much of this is attributable to base closures in the U.S. and overseas. However a great deal of the decrease has been through efficiencies in operation. For example, in 1996, DeCA outsourced their distribution to the private sector that decreased operating costs and returned nearly \$500 million to the stock funds of the DOD. In our prepared statement, we lay out the miniscule fraction of personnel costs and the overall defense budget that commissaries use and the high return that the DOD and the taxpayer realize from this investment. All of these facts have been outlined in several reports including a report commissioned by DOD to the Rand Corporation. The DOD and the Armed Services Committees of the House and Senate have stated that there should be no decrease in the level of savings that patrons realize by shopping at the stores. Because commissary costs have been cut so drastically over the years, it is difficult to see where costs can be cut without impacting the benefits to the patrons. DOD commissioned another study to look at reducing costs. The Boston Consulting Group identified several areas where they thought costs could be reduced. We have reviewed this report in detail. There are some efficiencies to be gained but major efficiencies outlined in the report require major changes to the system that have been enacted or implemented over many years. Each of the efficiencies in the report need to be closely examined and carefully implemented. Changes to purchasing and supply chain practices need to be carefully implemented considering the real world impact on existing relationships between manufacturers,

brokers and distributors and the disruption of promotions, deals and discounts that have grown up over the years. We certainly don't want to implement a program that results in gains in one area but corresponding losses on another side of the supply chain. Another major element of the BCG report is savings in employee salaries by making them nonappropriated fund employees. While there possibly could be some savings here, it will impact the existing pay and benefits of thousands of workers. The BCG report suggests new pricing models for patrons and introduction of private label in addition to the value brands that are already available in commissaries. Here, there need to be sold metrics to measure the impact to patrons before entering into any new arrangement. DOD is required to submit a report by March 1 on areas where they can gain efficiencies, using the BCG report and other sources. We look forward to reviewing this report and providing our views on areas where industry and the DOD can work cooperatively together with the dual goals of making the system as efficient as possible and not reducing the benefits to patrons.

Mr. JONES. Military compensation continues to receive considerable scrutiny. What are the major concerns identified by your constituents over commissary reforms?

Mr. GORDY. The primary concern for commissary reform is adverse impact any reforms may have on the benefit provided through the commissaries, particularly if prices are increased. Secondarily, if the benefit is diminished, we are concerned about the impact on traffic in the commissaries and, subsequently, in the exchanges.

Protecting the military resale ecosystem and the benefits they provide directly to the patron as well as indirectly through Morale, Welfare and Recreation programs is foundational.

The Armed Forces Marketing Council is very grateful to the Committee for establishing benchmarks for reform that would protect the benefit by maintaining consistent levels of savings.

We are also concerned about the introduction of private label products in the commissary, which would shift DeCA from an elegant, yet simple model of offering national brands at cost to a more complex and costly model of introducing private label products sold at a mark-up. Increased costs will come from the management and oversight personnel that will have to be employed to manage the program, as well as the shipping, stocking, and marketing of the products. We believe that this effort has been oversold as a means of reducing DeCA's appropriation and that a true, full-spectrum analysis has yet to be conducted to understand not only the direct costs of implementing such a program, but the indirect costs that will come as a result of industry partners reducing the in-store service and marketing and advertising support, which is not currently provided to other retailers.

Mr. JONES. What measurements should be imposed to determine if commissary reforms are beneficial or harmful to the commissary benefit?

Mr. GORDY. We believe that protecting the savings and model are key. Efficiencies can be achieved in DeCA without affecting the benefit.

Measurements should include what Congress has already established as benchmarks:

- 1—Provision of high quality products.
- 2—Maintain high-levels of customer satisfaction.
- 3—Sustainment of discount savings.

Even while these three benchmarks may be achieved while instituting reforms, it does not necessarily mean that patrons will continue to shop. Monitoring patron behavior in response to reforms is also important. If the reforms are discouraging patrons from shopping, then consideration for a quick reversal of the reform should be made.

Mr. JONES. Recognizing that there continue to be supporters of the privatization commissaries and zeroing out the appropriated funding, how would you propose to reduce the appropriated cost of commissaries?

Mr. GORDY. The AFMC does not believe the commissary benefit can be delivered without appropriated support. However, we do believe that reductions in the appropriation can be made through more efficient management of DeCA.

We believe there needs to be a rebalancing of the workforce between store-level and above-store-level staff. A review of above store-level staffing should be conducted to determine if requirements can be met with fewer staff.

We also cautiously support NAFing DeCA's workforce in order to balance pay in the commissary system with the civilian marketplace. This would mean some salaries would be reduced, while there would be some salaries that would be increased in order to attract top quality talent. While this may incur increased cost in the near term to establish new employee management systems (ie, retirement, healthcare, etc), over time it will deliver savings and more efficient and effective workforce.

We believe as DeCA fully implements its Enterprise Business System (EBS), which will replace its decades-old, antiquated system, less man-power and less contracted support will be required to input, manage and maintain its enterprise system. It will make working with DeCA more efficient for industry and result in less manually-entered data. Savings will be captured as the EBS comes on line in the near term and as additional elements of the system are deployed in the long term.

Mr. JONES. Military compensation continues to receive considerable scrutiny. What are the major concerns identified by your constituents over commissary reforms?

Ms. HUCK. In our view, and in the view of many military families, the savings that shoppers receive when shopping at the commissary is an important non-pay benefit. Commissary savings can be seen as part of the total military compensation package. Thus, any reform measure that would reduce the value of the savings is essentially a cut to military compensation. While these savings are important to all beneficiaries, they are especially critical to families living overseas or in remote or high cost locations, where there may be few affordable shopping options. Military families understand that the military resale system is complex and the various elements are interdependent. Changes to one aspect of the system may have unintended and unwanted influence on other areas. For example, the economies of scale generated by sales at high volume commissaries allow groceries to be sold at low cost across the system. Changes to the way high volume commissaries operate may threaten the economies of scale, leading to higher prices in those areas where shoppers are most dependent on the commissary. It must also be noted that in recent years military families have seen pay raises below the Employment Cost Index (ECI), caps to their Basic Allowance for Housing (BAH), and increased pharmacy co-pays. While each of these is insignificant on its own, taken together they represent a measurable loss in military families' purchasing power. Families are aware of these cuts, which makes them even more anxious about prospective reductions in commissary savings.

Mr. JONES. What measurements should be imposed to determine if commissary reforms are beneficial or harmful to the commissary benefit?

Ms. HUCK. The first and most important metric that should be used when analyzing any proposed reform to the commissary system is the impact it will have on savings. The current practice of selling goods at cost plus five percent gives families the assurance that they will be able to feed their families affordably wherever they happen to be stationed. Any change to the system must be measured against the level of savings currently available to families who shop at the commissary. The recent study by the RAND Corporation demonstrated that if prices increase military families will be less likely to shop at the commissary. Thus, we would recommend that any change to commissary operations be followed by an analysis of sales volume across the system. A drop in sales and/or the number of families using the commissary would indicate that the reform was harmful to the commissary benefit.

Mr. JONES. Recognizing that there continue to be supporters of the privatization commissaries and zeroing out the appropriated funding, how would you propose to reduce the appropriated cost of commissaries?

Ms. HUCK. We understand that reducing the commissary appropriation is a goal of many in the Department. In this era of fiscal restraint, it is reasonable to ask whether it is possible to reduce commissary funding without compromising the quality and value of the benefit and if so, how this might be accomplished. Our position has always been that any funding cuts should not be visible at the store level or affect military families' shopping experience. Military families worry that funding cuts will result in reduced operating hours or store closures. We urge Congress to oppose any reduction to the appropriation that would be apparent at the store level. Making it harder for military families to shop at the commissary is effectively a cut to the benefit and will paradoxically result in lower revenues as well. It may be possible to reduce the commissary appropriation by identifying changes to back-end operations that could lead to greater efficiency and lower cost. For example, as the Military Compensation and Retirement Modernization Commission (MCRMC) suggested, opportunities may exist to improve efficiency by consolidating certain operations with the military Exchanges. We would suggest exploring whether combining the organizations' headquarters, shipping, warehousing or other logistical operations would lead to significant savings without compromising the value of the benefit to service members and families. However, our Association does not have the expertise to make more specific cost-cutting suggestions. Organizations such as the American Logistics Association and the Armed Forces Marketing Council might be better placed to offer specific cost-cutting recommendations. While it may be possible to find efficiencies and reduce costs, it is the view of our Association that the commissary system as currently constructed effectively delivers a valuable benefit to

military families around the world. In our view, the commissary appropriation is money well spent as it helps ensure that even the most junior service members are able to feed their families. We caution against any change to the system that would threaten this essential benefit, which again is part of the total military compensation package.

Mr. JONES. Military compensation continues to receive considerable scrutiny. What are the major concerns identified by your constituents over commissary reforms?

Ms. GOLDBERG. Military families and other commissary patrons continue to be concerned that any reform will include degradation in the quality of products sold at the commissary, a reduction in access to the commissary (i.e., reduction in store hours) or an increase in prices. All of these are undesirable to patrons for obvious reasons. A decrease in patronage at the commissary will result in a similar decrease in traffic at Exchanges, which in turn means reduced funding for Morale Welfare and Recreation programs. Over the past years, Service budgets have significantly reduced funding to MWR programs, to include closures of specific MWR activities. Reducing the funding stream from Exchanges will further compound the budget challenges faced by the respective departments. This decrease in support programs could adversely affect morale, recruitment and retention.

Mr. JONES. What measurements should be imposed to determine if commissary reforms are beneficial or harmful to the commissary benefit?

Ms. GOLDBERG. We absolutely agree that the benchmarks set for reform in the FY16NDAA of maintaining product quality, savings and customer satisfaction at current levels (or better) are imperative. A comprehensive customer survey and refined market-basket comparison would contribute to a quantifiable assessment of commissary reforms and efficiency initiatives. In the end, any reform should be very carefully scrutinized and tested in those areas to determine if those benefit areas will be adversely affected.

Mr. JONES. Recognizing that there continue to be supporters of the privatization commissaries and zeroing out the appropriated funding, how would you propose to reduce the appropriated cost of commissaries?

Ms. GOLDBERG. We believe that supporters of privatization do not have a full understanding of the complexities involved. DOD leaders have acknowledged privatization while maintaining the benefit at current levels is not possible. When the benefit at the commissary is reduced, there is a trickle-down effect at the Exchange, and then a reduction in MWR dividends for support at the installation. DeCA may be able to find new ways to save operating costs, and we believe they are in the best position to do so. Any changes should not impact the product quality, savings, or customer satisfaction. Commissary access contributes to a very broad consumer base . . . active duty, family members and retirees—so any negative outcome of this reform will have a cascading effect well beyond the “currently serving” military population. Congress must be prepared to defend this benefit and appropriations at levels that preserve savings, quality, and customer satisfaction. Military families have seen reductions or stagnation in benefits across the board. This benefit (along with healthcare) is seen as a landmark benefit of military service. It has been linked to improved morale and we believe its erosion will be viewed as one more broken promise.