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STUDY OF MILITARY COMMISSARY STORES. VOLUME I

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FOREWORD

The study report has been prepared in two volumes (I and II). Volume I provides introductory and background information relating to the study, along with summary discussions of present service commissary systems, alternatives considered, conclusions and recommendations. Volume II is comprised of appendices providing detailed discussion and supportive data related to material contained in Volume I.

The study group extends its deeply felt gratitude to the many individuals and organizations, both governmental and private, who contributed their time and effort in providing suggestions and assistance to the committee.

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CHAPTER 1

INTRODUCTION

1-1. AUTHORITY FOR STUDY. This study was conducted in response to a directive issued by the Secretary of Defense and contained in Program/Budget Decision 282. Responsibility for direction of the study was assigned to the Assistant Secretary of Defense, Manpower and Reserve Affairs (M&RA), who promulgated a memorandum for the Assistant Secretaries of the Military Departments (M&RA), outlining the terms of reference to be followed during the conduct of the study. A copy of the ASD (M&RA) memorandum is at Appendix 1-A (p 1-3).

1-2. BACKGROUND.

a. By Program/Budget Decision 282, the Secretary of Defense proposed the elimination of direct appropriated fund support to commissary stores, for the costs of military and civilian employees, and for utilities. The utility costs would affect only those commissaries located overseas (plus Alaska), since those located within the continental limits of the United States and Hawaii are already required to reimburse appropriated funds for utility costs. The surcharge or selling prices applied to purchases by commissary patrons will be increased to cover these direct costs, thereby putting the commissary system on a type of financing akin to that used by the military exchange systems. Under the proposal, the direct subsidy for transportation to overseas areas will be continued along with indirect support costs (e.g., rent, building maintenance, installation/base administrative support, etc.). A copy of Program/Budget Decision 282 is at Appendix 1-B (p 1-7).

b. The transition to a self-supporting basis for direct costs would be phased over a 1-year period beginning on 1 October 1975. Effective on that date, reimbursement (to appropriated funds) of 50 percent of personnel and utilities costs would be required. On 1 October 1976, and thereafter, 100 percent of these costs would be reimbursed. Congressional appropriations to be reimbursed as a result of this realignment of funding are those for Operation and Maintenance (O&M), Research, Development, Test and Evaluation (RDT&E) and Military Personnel.

1-3. STATEMENT OF THE TASK. The principal task of the study group was to determine ways to improve the efficiency, organization, and operating structure of military commissary stores to assure continued savings to patrons, while at the same time providing for the reimbursement by the commissary system of direct personnel and utility costs previously supported by Congressionally appropriated funds. This task included the consideration of several alternatives listed below:

- a. Retention of the current system on a reimbursable basis,
- b. Creation of a service-wide commissary management organization to operate separate-service commissary stores,
- c. Establishment of common management organizations for exchange and commissary operations for the respective military service,
- d. Creation of one agency to operate all commissary stores within DOD, and
- e. Operation of commissary stores under a GOCO (Government-owned, contractor-operated) arrangement.

1-4. OBJECTIVE OF THE STUDY. The objective of the study, as stated in the memorandum setting forth the terms of reference (App 1-A, p 1-3), was to determine what changes, if any, should be made to the military commissary store system in its organization and operating structure for improved efficiency, reduced costs and better service to the patrons.

1-5. MEMBERSHIP OF STUDY GROUP. In accordance with the memorandum from the Assistant Secretary of Defense (Manpower and Reserve Affairs), which set forth the terms of reference for the study, the various services nominated individuals to serve on the committee. During the course of the study, additional members were included, on either a full or on-call basis, to represent particular organizational activities (e.g., Defense Supply Agency), or to provide certain technical expertise (e.g., Civilian Personnel Administration and Public Affairs). The composition of the study group is shown at Appendix 1-C (p 1-15).

1-6. DEFINITIONS. Definition of some key terms used in the study are shown in Appendix 1-D (p 1-8).

1-7. ABBREVIATIONS. The abbreviations for various terms used within the study report are identified in Appendix 1-E (p 1-20).

APPENDIX 1-A

ASSISTANT SECRETARY OF DEFENSE (M&RA) MEMORANDUM



MANPOWER AND
RESERVE AFFAIRS

ASSISTANT SECRETARY OF DEFENSE
WASHINGTON, D. C. 20301

30 JAN 1975

MEMORANDUM FOR The Assistant Secretaries of the Military
Departments (M&RA)

SUBJECT: Terms of Reference for Study of Military Commissary Stores

By Program/Budget Decision 282, the Secretary of Defense directed that a study be conducted, under the direction of this office, to determine the ways to improve the efficiency, organization and operating structure of military commissary stores. This memorandum specifies the terms of reference for a joint Service study of military commissary stores of the Department of Defense.

The objective of this study is to determine what changes, if any, should be made to the military commissary store system in its organization and operating structure for improved efficiency, reduced costs, and better service to the patrons. Possible considerations include, but are not limited to the following:

- 1) Creation of Service-wide commissary management organization to operate Service commissary stores.
- 2) Establishment of common management organizations for exchange and commissary operations for the respective Military Service.
- 3) Creation of one agency to operate all commissary stores within DoD.
- 4) No change to current structure.

The following positions on the joint Service study group require nominations from addressees:

Department of the Army

- 1) Chairman - A general officer with a thorough background in military logistics, particularly in regard to commissary stores and support services.

2) Two commissary specialists - may be military or civilians who have or are currently performing commissary staff or management duties at the Departmental or sub-Departmental level.

3) Comptroller member.

4) Exchange representative.

Department of the Navy

1) Vice Chairman - A Captain or Colonel with similar type experience as the Chairman.

2) Three commissary specialists, including a Marine Corps representative - may be military or civilians who have or are currently performing commissary staff or management duties at the Departmental or sub-Departmental level.

3) Comptroller member.

4) Exchange representative.

Department of the Air Force

1) Two commissary specialists - may be military or civilians who have or are currently performing commissary staff or management duties at the Departmental or sub-Departmental level.

2) Comptroller member.

3) General Counsel - military or civilian attorney.

In addition to the initial personnel requirements from the Military Departments, there may be other requests for specialists as required during the course of the study, such as manpower specialists. Such support will be requested by the Chairman and approved by ASD(M&RA).

A full-time administrative staff, including an executive secretary and clerical support as determined necessary by the Chairman will be provided and equitably shared by the Military Departments. The

Department of the Army will provide office space and equipment in the Washington, D. C. area for the study group and staff. Any funds required for the study effort will be from those available to each Department concerned.

Departmental nominations, with individual qualifications, will be provided to this office by February 8, 1975.

It is desired that the final report, to include Military Departmental reviews, be submitted to this office by May 30, 1975.

(signed) William K. Brehm

APPENDIX 1-B
PROGRAM/BUDGET DECISION 282

PROGRAM/BUDGET DECISION		NUMBER 282				
Commissary Stores		Department of Army, Navy, Marine Corps, Air Force				
Covers all the appropriated funds to support the DoD commissary stores.						
	FY 1974	FY 1975	FY 1976	FY 1977	FY 1977	
Service Estimate, TOA \$ Mil.	262.6	272.7	293.9	73.0		
Service Estimate, Mil. E/S	2,083	2,219	2,220	2,220	2,220	
Service Estimate, Civ. E/S	25,240	25,186	25,474	25,474	25,474	
Alt. Est. No. 1, TOA \$ Mil.	262.6	269.8	281.6	67.6		
Alt. Est. No. 1, Mil. E/S	2,083	2,164	2,083	2,028	1,934	
Alt. Est. No. 1, Civ. E/S	25,240	24,549	23,562	23,277	22,156	
Alt. Est. No. 2, TOA \$ Mil.	262.6	269.8	228.5	40.8		
Alt. Est. No. 2, Mil. E/S	2,083	2,164	1,420	1,289	1,221	
Alt. Est. No. 2, Civ. E/S	25,240	24,549	14,867	14,686	13,942	
Alt. Est. No. 3, TOA \$ Mil.	262.6	269.8	175.6	32.0		
Alt. Est. No. 3, Mil. E/S	2,083	2,164	1,420	1,289	1,221	
Alt. Est. No. 3, Civ. E/S	25,240	24,549	14,867	14,686	13,942	
Alt. Est. No. 4, TOA \$ Mil.	262.6	271.5	78.7	1.3		
Alt. Est. No. 4, Mil. E/S	2,083	2,219	2,220	2,220	2,220	
Alt. Est. No. 4, Civ. E/S	25,240	25,186	25,474	25,474	25,474	
Alt. Est. No. 5, TOA \$ Mil.	262.6	272.7	186.3	37.2		
Alt. Est. No. 5, Mil. E/S	2,083	2,219	2,220	2,220	2,220	
Alt. Est. No. 5, Civ. E/S	25,240	25,186	25,474	25,474	25,474	
Evaluation: The existence of commissaries in the military life dates back to 1867 and originated when military installations were located in the wilderness of the United States, and the military personnel were grossly underpaid. During the intervening years the commissaries have come to be viewed as an "implied contract" by the military personnel. However, during the intervening years the conditions requiring their existence have radically changed.						
Alternative No. 1 proposes the retention of appropriated fund support of all commissaries, but requires a productivity improvement of 15% in personnel supported by appropriated funds over a 3 year period starting 1 January 1975.						
Alternative No. 2 includes Alternative 1 adjustments and proposes the closing of 133 of the 284 CONUS commissaries by January 1, 1976, and financing the remaining CONUS and overseas stores with appropriated funds.						
Alternative No. 3 includes the adjustments in Alternative 2 and, with the exception of overseas transportation costs, proposes the substitution of surcharge funds for the remaining appropriated funds over the period FY 76-FY 78.						
Alternative No. 4 proposes the retention of all existing commissaries and, with the exception of overseas transportation costs, the substitution of surcharge funds for the appropriated fund support on 1 October 1975. It also proposes the study noted in the detail of evaluation.						
Alternative No. 5 proposes phasing Alternative No. 4 over a two year period, with reimbursement from the commissary surcharge as follows (\$ in millions).						
	FY 1976	FY 1977	FY 1977-80			
Reimburse the O&M and RDT&E appropriations	107.578	35.831	260.916			
Reimburse the Mil. Pers. appropriations	-	-	25.961			
Alternatives No. 3, 4 and 5 require a change to Sec. 814 of the General Provisions, Outyear impact: Discussed in the Detail of Evaluation.						
Alternative No. 1	Approve the TOA and personnel E/S shown in table above.					
Alternative No. 2	Approve the TOA and personnel E/S shown in table above.					
Alternative No. 3	Approve the TOA and personnel E/S shown in table above.					
Alternative No. 4	Approve the TOA and personnel E/S shown in table above.					
Alternative No. 5	Approve the TOA and personnel E/S shown in table above.					
DECISION						
The Secretary approved alternative 5. December 19, 1974						

CONTINUATION OF CONSIDERATION

BACKGROUND

The earliest identified reference to this type of service is an Appropriation Act of 1866 which authorized the Subsistence Department of the Army "... to furnish such articles as may from time to time be designated by the inspectors general of the Army, the same to be sold to officers and enlisted men at cost prices..." starting July 1, 1867. The origins of commissary stores are mentioned in a report of the Naval Affairs Committee of 1932. It stated, "Existing Army and Navy exchanges, and commissaries had their origin in the canteens established to meet the personal and other requirements of enlisted men because of the isolation and inaccessibility of certain Army posts principally in the unsettled areas of the West, and because of the long voyages in past years of battleships and other fighting craft."

The conditions surrounding the origin of commissary stores no longer exist today. They started as a convenience in isolated areas of the country. As the country became more settled and as military pay remained low, the economic benefit rather than convenience was stressed. The economic benefit of commissaries to the patrons is that prices are about 22% below those in grocery chain stores.

The direct subsidy of commissaries for the payroll costs of military and civilian employees constitutes about 10% of this 22% savings to commissary patrons. The other 12% is attributable to subsidized indirect costs, such as rent, maintenance, and administrative support; lower wholesale costs to commissaries of certain items, principally dairy products and produce; and elements of cost not applicable to commissary stores, such as advertising, taxes, insurance, and profits.

Magnitude

The magnitude of commissary operations worldwide can be illustrated by the Service estimates of the following data for 1976:

Number of stores	426
Military and civilian end strengths	27,715
Sales (\$ in millions)	2,952

In addition to labor-related costs, commissaries are also subsidized by appropriated funds for utilities costs at overseas stores, transportation costs to overseas areas, and for indirect costs such as space occupancy and base support services which LMI in a study of commissaries estimated to be in the range of 4.8-8.25% as a percent of sales. Appropriated funds have in the past been used to construct commissaries. However, present DoD policy is that they will now generally be financed through a surcharge on price of the goods. Enabling legislation is contained in the Senate version of the Military Construction Authorization Bill for 1975. Besides these appropriated funds, surcharge collections (paid by the customer) required by a General Provision in the annual DoD Appropriation Act are used to finance certain specified elements of cost such as equipment and supplies. This present surcharge ranges from 2½ to 5%.

Patronage

At any base, commissary privileges are available not only to military personnel and their dependents stationed at the base, but also to all active duty personnel and their dependents of any uniform service. In addition, retired personnel and widows of retired personnel may use the commissary. No detailed survey data exists as to

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Budget released 2 mos. ago 11 Jul 75

CONTINUATION OF CONSIDERATION

the exact composition of commissary patronage, but spot checks taken from time to time indicate that 45-50% of commissary customers are retired personnel or their dependents, with the balance being active duty personnel and their families who for the most part represent career committed individuals with longer service and higher grades. On a straight extrapolation, retirees can be expected to constitute over half the commissary patrons in a few years.

Certification Criteria

To continue operating commissaries in CONUS, the Secretary of Defense is required, by law, to certify that, "... items normally procured from commissary stores are not otherwise available at a reasonable distance and a reasonable price in satisfactory quality and quantity..." The criteria established by DOD to evaluate these factors have not changed since 1949. It is significant to note that in no case, since the establishment of criteria was required by law, has a CONUS commissary been closed for not meeting these criteria. Alternatives No. 2, 3, and 4 would require the criteria to be changed.

DETAIL OF EVALUATIONAlternative 1

The management of the DoD commissaries has initiated many actions to improve the productivity and operating efficiency of their stores. Examples of the improvements they have been making are listed in point style below:

- . Automation through the use of computers.
- . Reducing overhead by redesignating stores as branches.
- . Establishing central warehouses to serve commissary stores in the general area.
- . Standardizing job descriptions - equalized pay scales.
- . Standardizing commissary store design.
- . Renovating projects to improve operations.
- . Procuring labor saving equipment of various types.

In addition to the above the managers are investigating the use of "Point of Sale Registers" which would employ an optical scanner to read the "Universal Product Code" that is currently being recorded on many consumer products, particularly food products. This relatively new innovation which is being tested by some commercial supermarkets will substantially improve the productivity of supermarkets. It will increase checker (at the register) productivity, automate and thereby reduce the price marking and reprice marking that is now done by hand. In addition to these direct and more readily identifiable savings there will be other savings through improved management of such functions as stock and inventory control. A recent study of McKinsey & Co. resulted in this statement: "Some people, including the McKinsey team, believe these soft savings may eventually be more significant than hard or productivity savings identified to date." The Service managers of the DoD commissaries are investigating this new procedure and are planning to install it if the tests produce the expected results. As a matter of fact portions of the new systems, i.e. employing a cash register as a remote to a computer are already in operation at several commissaries. The productivity improvements (hard savings) of the complete systems should lead to net savings before tax equal to 1.0 to 1.5 percent of sales, and this is a "people savings" without considering the "soft savings"

CONTINUATION OF CONSIDERATION

referred to above. The "hard savings" would involve approximately a 15 percent productivity improvement.

The commissary surcharge finances equipment investments, and as indicated in the following table, these investments have been substantial over the last few years:

DoD Commissary Investments in Equipment

	<u>\$ in Millions</u>	
	<u>Year</u>	<u>Cumulative</u>
FY 1973	15.9	
FY 1974	16.6	32.5
FY 1975	23.3	55.8
FY 1976	22.9	78.7

While most of the above investments, no doubt, represent the replacement of equipment that does not materially contribute directly to increased productivity, the Services have indicated that a currently unknown portion of these procurements have been for labor savings equipment. Without considering the other productivity improvements mentioned in the first paragraph, one-third of the equipment investments over a three year amortization period would produce a productivity savings of approximately 5% per year. This does not include investments in the "Point of Sale Register" concept described above.

Notwithstanding the above, the Service estimates reflect stable employment levels and do not consider changes from productivity improvements. A productivity improvement affecting direct and indirect employment of 15% over a three year period appears reasonable and this was the basis for the Alternative No. 1 proposal.

Alternative 2

On 30 June 1974 there were 286 CONUS and 144 overseas commissaries. A recent survey of the CONUS stores indicates that 133 of these stores are located within approximately 10 minutes driving time to the nearest commercial supermarket. This same survey indicates that 194 were within 15 minutes driving time and 6 were 45 minutes or more from the nearest commercial supermarket. There is recent evidence of mounting Congressional pressure to eliminate this duplication of facilities when commercial stores are reasonably accessible. The proposal in Alternative No. 2 to close those stores that are within a reasonable distance from commercial supermarkets is not based solely on the Congressional attitude, or the recent publicity in the press, but also on the premise that it is economically wasteful to the nation to duplicate Government owned and operated and private owned and operated facilities. The military installations are no longer located in the wilderness and it appears logical to now consider closing those commissaries that are within 10 minutes of commercial supermarkets. At some future time it might be appropriate to consider closing those that are a little further away from privately operated stores. Since the commissaries are an instrumentality of the Federal Government they are not required to pay income taxes and related fees nor to charge their customers sales taxes. The revenue lost to the Federal, State and Local Governments is estimated to amount to over \$150 million annually, and this is an additional factor that should be considered. Alternative No. 2 includes an appropriately factored portion of Alternative 1 and proposes closing those commissaries that are within approximately 10 minutes driving time to the nearest supermarket. Alternative No. 2

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continues to use appropriated funds to support the remaining COMUS commissaries and all of those located overseas. It is reasonable to assume from recent events that unless DoD management takes some appropriate action in this direction the Congressional Appropriation Committees may take the initiative.

Alternative 3

This alternative involves the adjustments in Alternative No. 2, and in addition proposes the withdrawal of appropriated funds supporting the commissary store operations over a three year period. As an exception Alternative 3 continues appropriated fund support for the costs involved in transporting the commissary goods overseas. Since military compensation has achieved comparability with compensation in the civilian sector there should no longer be a requirement to further subsidize military pay with appropriated funds to reduce their food expenses. It may be appropriate, in taking this action, to consider the phased withdrawal of appropriated fund support. A phasing of this action would permit: (1) time to formulate and implement an appropriate top management structure to control this approximate \$3.0 billion business, (2) permit the revised management structure time to consider the continuing requirement for some of the remaining commissaries, and (3) permit the management to raise the surcharge rates to nearly a self sufficient operating level on a phased basis giving consideration to those "plow back" investments considered appropriate to achieve an optimum operating efficiency. Considering the above rationale the three year phasing period proposed in Alternative 3 appears reasonable.

Alternative 4 and 5

This alternative would eliminate the direct subsidy to commissary stores for the costs of military and civilian employees and utilities. It also directs a study with results to be available by May 30, 1975, in an effort to improve the efficiency, organization, and operating structure of commissary stores.

Previously, the economic advantages of the commissary system were related to the relatively low pay of military personnel. However, that condition no longer exists. As stated in the report of the Senate Appropriations Committee on the 1975 DoD Appropriation Act, "...the military are supposed to have achieved salaries comparable to those paid to civilians." The present military pay structure has been raised to compete with the civilian sector in recruiting and retaining personnel. It is tied to comparability with salaries and wages paid in the private sector, and periodic upward adjustments to military pay are made to maintain this comparability. The value of the commissary privilege plays no part in such adjustment and, as stated in the staff report of the First Quadrennial Review of Military Compensation, is an inappropriate element of compensation. The value of the benefit varies with size of family, income, availability of commissaries, and frequency of use. Its value as an inducement to AVF recruits seems marginal since most are single and would seldom use the commissaries; its attractiveness to career committed personnel is obviously greater.

This alternative would eliminate the direct subsidy, effective October 1, 1975, the date on which the next pay adjustment is scheduled. Under this alternative, appropriated funds would no longer be available for this element of cost and the surcharge would be increased to recover this cost. Section 814 of the General Provisions in the DoD Appropriation Act would be amended in the 1976 budget to

PROGRAM/BUDGET DECISION (Continuation)	NUMBER 282
CONTINUATION OF CONSIDERATION accomplish this change in financing. This change would place commissaries under a type of financing similar to that applicable to exchange stores. For commissary patrons, sales prices would be increased by about 10%; however, they would still be 10-12% lower than commercial stores. The direct subsidy for transportation to overseas areas would be continued as well as the indirect subsidies for all stores such as rent, maintenance, and administrative support. In addition to the above reductions, funding for supplies and equipment is deleted since existing law requires these costs to be financed by the surcharge. The report of the House Appropriations Committee on the 1975 DoD Appropriation Act questioned the overall management of commissary operations and requested a GAO review of the area. It stated that, "The management of commissary operations has never been reviewed Department-wide by Defense audit/management organizations." An OMB study of commissaries revealed a number of opportunities which appear to offer improvement in the operation of commissaries. In total, commissary store sales rank them among the largest chain stores in the country. Unfortunately, many commissaries are run on an individual store basis. The Navy operates in a centralized manner whereby stores in a geographical area are grouped into a "complex." Marine Corps commissaries exist as independent stores due to both the small number of stores and wide geographical distances. The Army and Air Force commissaries exist primarily as independent stores and could benefit both administratively and economically from a greater degree of centralization. The Navy system and experience also points to the opportunities for operating economies in areas such as centralized warehousing and meatcutting. Other than two Navy locations, centralized warehousing on a regional or area basis are not the practice. Yet, centralized warehouses provide the opportunity for bulk lot purchasing and reduce inventory, manpower and transportation costs. A centralized meatcutting plant, being built for the Norfolk complex through surcharge funds, is estimated by Navy to be able to produce initial annual operating savings of \$200,000, with the potential for additional annual savings of \$250,000. Grocery chains have used these types of centralized operations for years. This effort to centralize existing service commissary operations should also examine the natural extension of four centralized systems into a single Defense commissary system with operating responsibility for all DoD commissary stores. The values which accrue from more centralized systems at the Service level could be even more effectively marshalled under a single Defense manager. Large, nationwide grocery chains operate hundreds of individual stores, and the benefits from central management of the 426 existing stores could be impressive. A study under the direction of the Assistant Secretary of Defense (M&RA) should focus on the most efficient method of operating commissaries. Due to the need to respond to expected Congressional criticism of the present method of operations, results of this study should be available by May 30, 1975.	

NECESSARY STOPS PROGRAM BUDGET DECISION (Continuation)		NUMBER 282			
CONFIRMATION OF CONSIDERATION		OUTYEAR ADJUSTMENTS			
		FY 1977	FY 1978	FY 1979	FY 1980
<u>Service Submit</u>					
TOA \$ Thousands	292,288	292,288	292,288	292,288	292,288
Civilian End Strength	25,474	25,474	25,474	25,474	25,474
Military End Strength	2,220	2,220	2,220	2,220	2,220
<u>Alternative No. 1 Allowance</u>					
TOA \$ Thousands	263,765	256,786	255,245	255,245	255,245
Civilian End Strength	22,154	21,661	21,650	21,650	21,650
Military End Strength	1,934	1,889	1,889	1,889	1,889
<u>Alternative No. 1 Reductions</u>					
TOA \$ Thousands	28,523	35,502	37,043	37,043	37,043
Civilian End Strength	3,341	3,834	3,845	3,845	3,845
Military End Strength	286	331	331	331	331
<u>Alternative No. 2 Allowance</u>					
TOA \$ Thousands	158,877	153,994	152,924	152,924	152,924
Civilian End Strength	13,942	13,546	13,535	13,535	13,535
Military End Strength	1,221	1,183	1,183	1,183	1,183
<u>Alternative No. 2 Reductions</u>					
TOA \$ Thousands	133,411	138,294	139,364	139,364	139,364
Civilian End Strength	11,553	11,949	11,960	11,960	11,960
Military End Strength	999	1,037	1,037	1,037	1,037
<u>Alternative No. 3 Allowance</u>					
TOA \$ Thousands	84,850	43,920	5,411	5,411	5,411
Civilian End Strength	13,942	13,546	13,535	13,535	13,535
Military End Strength	1,221	1,183	1,183	1,183	1,183
<u>Alternative No. 3 Reductions</u>					
TOA \$ Thousands	207,438	248,368	286,877	286,877	286,877
Civilian End Strength	11,553	11,949	11,960	11,960	11,960
Military End Strength	999	1,037	1,037	1,037	1,037
<u>Alternatives No. 4 and 5 Allowance</u>					
TOA \$ Thousands	5,411	5,411	5,411	5,411	5,411
Civilian End Strength	25,474	25,474	25,474	25,474	25,474
Military End Strength	2,220	2,220	2,220	2,220	2,220
<u>Alternatives No. 4 and 5 Reduction</u>					
TOA \$ Thousands	286,877	286,877	286,877	286,877	286,877
Civilian End Strength	0	0	0	0	0
Military End Strength	0	0	0	0	0

APPENDIX 1-C

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APPENDIX 1-C

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APPENDIX 1-D

DEFINITIONS

1. Administrative Support. This encompasses support such as finance and accounting services, military personnel, administration, mail pick-up and delivery, civilian personnel services, legal services, safety, and comptroller services.
2. Commissary Officer. That person in the Army or Air Force organizational structure at post or base level who is responsible for the management of the troop issue function and the commissary store function.
3. Commissary Store Officer. That person responsible for the management of the post, base or station commissary store.
4. Cost Factors. In order to compute and analyze the economic impact of various organizational and funding alternatives for the management and operation of commissary stores, cost was divided into three basic cost factors - personnel, operations, and capital outlay. Personnel costs include all salaries and benefits. Operating costs include all costs other than personnel and capital outlay costs and include such things as materials, services, utilities, minor equipment, operating supplies, shrinkage, etc. Operational costs can be both fixed and variable and include commissary store costs and operational costs above store level. Capital outlays include all costs associated with construction, renovation, and major equipment procurement for commissary stores.
5. Direct and Indirect Costs. Each service for each alternative considered has used different assumptions regarding the definition of direct and indirect costs, determined, largely, by their current degree of centralization. Because of the differences in organizational structure of each of the service's commissary store systems this different interpretation of direct and indirect costs was required. Basically, direct costs are those expenses that can be directly associated with the operation of the commissary store and would not be incurred if the commissary store were abolished. Indirect costs are those expenses from support oriented programs which are independent of the existence of the commissary store, cannot be specifically identified with the operation of the commissary store, and would continue at a lower level of magnitude, if the commissary store were abolished. Indirect cost would include such items as space occupancy (rent), base support services, building exterior maintenance, and administrative support.

6. Equivalent Supermarket Sales. This is the dollar value, less state and local taxes, that would have to be paid in a commercial supermarket to purchase an equal quantity and quality of merchandise sold by a military commissary store.

7. Mark-on/Markup. These two terms were used synonymously in the study. Markup is the difference between the cost price and the selling price of an item, computed as a percentage of the selling price.

8. Price Differential. This is the difference between the cost price of an item in the military commissary store and the selling price (less taxes) of that same item in a commercial supermarket, computed as a percentage of the military commissary store cost price. To derive price differential, it is often weighted by the Department of Labor's weighting factors.

9. Sales. This is the dollar value of items sold in the military commissary stores. In the Army and Air Force, this dollar value does not include their surcharge. In the Navy and Marine Corps, the dollar value includes its markup. For the economic analysis portion of the study commissary store sales include mark-on and/or surcharge.

10. Savings. This is the difference between the selling price (including mark-on/surcharge) of an item in the military commissary store and the selling price (less taxes) of that same item in a commercial supermarket, computed as a percentage of the commercial supermarket selling price.

11. Section 814 Annual DOD Appropriation Act. This is that portion of the Annual DOD Appropriation Act that specifies the costs that the military commissary stores must pay from surcharge or markup. Currently, it is Section 814; however, the reference number changes from year to year.

12. Surcharge. This term is used by the Army and Air Force commissary store programs. It is the factor, expressed as a percentage, that is applied against the price of an item sold in the commissary store. For Army, it is currently 3.0 percent in CONUS and Hawaii, and 2.5 percent overseas. For the Air Force, it is 3.0 percent.

13. TRFA/CSRF. An abbreviation referring to the Army and Air Force Trust Revolving Fund Account and the Navy's Commissary Store Reserve Fund.

APPENDIX 1-E

ABBREVIATIONS

AAC - Alaskan Air Command
AAFES - Army and Air Force Exchange Service
ACMIS - Army Commissary Management Information System
ADC - Air Defense Command
ADP - Automatic Data Processing
A&E - Architectural and Engineering
AFB - Air Force Base
AFCMO - Air Force Commissary Management Office
AFLC - Air Force Logistics Command
AFSC - Air Force Systems Command
AFSO - Air Force Services Office
ALA - American Logistics Association
AMIS - Automated Management Information System
AOB - Approved Operating Budget
ASCSR - Armed Services Commissary Store Regulations
ASF - Army Stock Fund
ATC - Air Training Command
CAC - Control Analysis Corporation
CGS - Cost of Goods Sold
CIVPERS - Civilian Personnel
CMO - Central Management Office
COMSYSTO - Commissary Store
CONUS - Continental United States (excludes Hawaii and Alaska)
CSA - Commissary Store Agency
CSMO - Commissary Store Management Office
CSO - Commissary Store Office
CSRF - Commissary Store Reserve Fund
DA - Department of the Army
DCSLOG - Deputy Chief of Staff for Logistics
D Day - Decision Day
DICOMSS - Direct Commissary Support System
DOD - Department of Defense
DPSC - Defense Personnel Support Center
DSA - Defense Supply Agency
EPOS - Electronic Point-of-Sale
ESIS - Electronic Store Information System
FAD - Funding Authorization Document
F&AO - Finance and Accounting Office
FF&V - Fresh Fruits and Vegetables
FOB - Free on Board
FPM - Federal Personnel Manual
HQ COMD - Headquarters Command

HQMC - Headquarters Marine Corps
 ICAR - Integrated Cost Accounting and Reporting
 IMM - Integrated Material Manager
 IMU - Initial Markup
 JSCSA - Joint Service Commissary Store Agency
 LMI - Logistic Management Institute
 MAC - Military Airlift Command
 MAJCOM - Major Command
 MCA - Military Construction, Army
 MCSA - Marine Corps Supply Activity
 MCSF - Marine Corps Stock Fund
 MILPERS - Military Personnel
 MIS - Management Information System
 MILSTAMP - Military Standard Transportation and Movement Procedures
 MPA - Military Personnel, Army (a Congressional appropriation)
 MPAF - Military Personnel, Air Force (a Congressional appropriation)
 MPMC - Military Personnel, Marine Corps (a Congressional appropriation)
 MPN - Military Personnel, Navy (a Congressional appropriation)
 M&RA - Manpower and Reserve Affairs
 NAF - Non-appropriated Fund(ed)
 NAFA - Non-appropriated Fund Activity
 NAVFAC - Navy Facilities Engineering Command
 NAVRESO - Navy Resale System Office
 NAVSUP - Navy Supply Systems Command
 NCR - National Cash Register, Inc.
 NEX - Navy Exchange
 NRSO - Navy Resale System Office
 O/A - Obligation Authority
 ODAB - Office, Director Army Budget
 OIC - Officer-in-Charge
 O&M Funds - Operation and Maintenance, followed by Service to which they
 pertain (i.e., O&M Army, O&M Navy, etc.)
 OMB - Office of Management and Budget
 OSD - Office, Secretary of Defense
 OSHA - Occupational Safety and Health Act
 PACAF - Pacific, Air Force
 PBD - Program/Budget Decision
 P&C - Purchasing and Contracting
 POA&M - Plan of Action and Milestones
 RDTE - Research, Development, Test and Evaluation (appropriation)
 RIF - Reduction in force
 SAC - Strategic Air Command
 TAC - Tactical Air Command
 TAD - Temporary Additional Duty
 TRFA - Trust Revolving Fund Account
 USAF - US Air Force
 USAFE - US Air Force Europe
 USAMMAE - US Army Materiel Management Agency, Europe
 USATSA - US Army Troop Support Agency

USMC - US Marine Corps
USN - US Navy
VPR - Voluntary Price Reduction
VDS - Vendor Drop System
VRR - Visual Rapid Reader System
WIMS - Worldwide Integrated Management System

CHAPTER 2

EXECUTIVE SUMMARY

2-1. OBJECTIVE. By Program Budget Decision 282, the Secretary of Defense directed the elimination of the appropriated fund support to commissary stores for the cost of civilian employees, military personnel, and overseas utilities. He also directed that a study be conducted to determine ways to improve the efficiency, organization, and operating structure of military commissary store systems. The Assistant Secretary of Defense (M&RA), by memorandum of 30 January 1975 to the Military Departments, established terms of reference for the study. The objective was to determine what changes, if any, should be made to the military commissary store system in its organization and operating structure for improved efficiency, reduced costs, and better service to the patrons. The members of the study group, representing each of the Services, were selected based upon their assignment and qualifications in staff and field operations in military retail sales.

2-2. AREAS OF CONSIDERATION.

a. The considerations in fulfilling the study objective ranged from retaining the present commissary store systems on a reimbursable basis through the following alternatives:

(1) Alternative 1 - centralized separate-Service commissary management system on a reimbursable basis.

(2) Alternative 2 - merger of the Services commissary store systems with their existing exchange systems.

(3) Alternative 3 - joint Service commissary store system on a reimbursable basis.

(4) Alternative 4 - government owned, contractor operated system.

b. Each of the alternatives was evaluated by review of the Services current commissary store systems, extensive participation and information from the commercial grocery industry, and previously conducted studies concerning both commissary and commercial grocery systems.

2-3. COMPLEXITY OF THE PROBLEM. It is difficult to determine the most efficient management structure and method of operation for commissary stores. The geographical dispersion and sizes of current stores - from \$5,000 in sales per month to more than \$2 million in sales per month - add to the complexity. Differences in current

management structures, methods of operations, and in proposed funding methods, using either appropriated or non-appropriated funds, compound the problem.

2-4. POTENTIAL AREAS FOR IMPROVEMENT. Operations and management could be improved to enhance efficiency and service. Urgent requirements exist for development and implementation of ADP systems for the Services. Systems installed must be capable of handling the high volumes of transactions in a central management mode which will meet requirements for intensified management and reduce administrative costs. Accounting and management information systems need to be developed as a prerequisite to developing ADP hardware and software requirements. Overhead costs can be reduced by consolidation of functions. Manning controls must be modified to permit greater utilization of employees to more effectively match manning to workload. An intern program needs to be developed that will provide adequate numbers of personnel qualified in commissary store management. Functional training needs to be stressed. Standards for measuring production efficiency need to be developed and implemented. Substantial improvements in facilities are required.

2-5. KEY FACTORS IN EXAMINING EACH ALTERNATIVE.

a. Selective functional consolidations, which offer significant potential savings were examined, particularly in such areas as command and control, administration, procurement, accounting, and distribution.

b. Two basic methods of funding were considered. These are reimbursement of appropriated funds and conversion to non-appropriated funding. These methods of funding impact differently on personnel and on direct and indirect costs.

c. Alternatives were also analyzed to determine total costs, i.e., direct and indirect costs. Direct costs were sub-divided into three categories: personnel, operations, and capital outlay. Examination of both direct and indirect costs was necessary because they are allocated differently under various alternatives. Indirect costs were estimated since no precise quantification of these costs exists. The study used constant FY 1975 dollars and existing policies/circumstances for purposes of analyses.

d. Reimbursement for personnel and overseas utilities costs will reduce savings to patrons from the present 22 percent. Reduced savings will result in reduced sales. The uncertainty lies in how much these reductions in sales and savings will be. Study group estimates pre-suppose effective customer communications as one of several measures that will minimize the impact of these factors.

e. The following Table depicts the estimated costs and savings for each alternative.

ESTIMATED COSTS AND CUSTOMER SAVINGS FOR PRESENT
SYSTEM AND EACH ALTERNATIVE BASED ON FY 1976
BUDGET PROPOSAL (PBD 282)

	Fiscal Year 1978 (\$ in millions)			Estimated Savings Percent (Note - 2)
	Estimated Costs <u>1</u> / Direct	Indirect	Total	
Present System	373.5	158.5	532.0	11.2 - 14.0
Alternative 1 - Centralized Separate Service Systems	353.6	144.5	498.1	12.5 - 14.7
Alternative 2 - Merger of Comsy/ Exchanges	432.8	110.5	543.3	11.9 - 14.2
Alternative 3 - Joint Service Commissary System	337.1	140.1	477.2	13.4 - 14.3
Alternative 4 - Government Owned, Contractor Operated	Analyzed by percent			0 4.4

Note 1 - Indirect cost does not include oversea transportation.

Note 2 - Ranges depicted for the present system and alternatives 1 and 2 represent the high or low result of all Services. Refer to separate chapter for specific estimates for individual Services.

2-6. MAJOR CONCLUSIONS.

a. Economies obtainable appear to be sufficient to permit reimbursement for direct costs as proposed, retain significant savings for customers, and maintain a workable commissary system. This conclusion is based on the assumed effective implementation of management, accounting, pricing, customer information, ADP, personnel, and statutory changes addressed in detail within this report.

b. The time constraint imposed for the commissary system to achieve the capability to reimburse for 100 percent of personnel and overseas utility costs, severely inhibits the orderly implementation of each alternative. Timely application of resources and implementation of actions necessary are essential to ensure the retention of customers and maximum customer savings.

c. Responsibility for troop issue is a command function. Under the self-sustaining concept, precise identification of costs, properly charged to both the troop issue and commissary store functions, is essential. The Services concerned should develop procedures which will

ensure equitable reimbursement for support provided by one entity (commissary store or troop issue) for the other.

d. Alternative 1 (Centralized Management Within Each Service) has the least impact on both patrons and commissary personnel of all alternatives examined. Each service has the capability to achieve centralized management within the time frame imposed with the least service at adequate levels. Also, this alternative keeps the services' options open until the full impact of PBD 282 is felt and customer reactions can be determined with certainty. If adopted, Alternative 1 requires priority actions to develop and implement necessary control mechanisms and requisite management and information systems.

e. Alternative 2 (Merger with the Exchange Systems), depending upon the method of allocating overhead costs and other income, could provide marginally lower savings to the patron than those obtainable under Alternatives 1 and 3. The Army and Air Force Exchange Service has an automated data processing system which, with appropriate modification, could support commissary requirements. This alternative would provide flexibility in management of personnel, provide a wide base for career progression, and produce system efficiencies as a result of the merger. This alternative could result in major personnel turbulence at the time of merger plus a substantial loss of existing managerial/supervisory personnel. Moreover, possible transfer of procurement support from DPSC to the exchange Services would adversely impact the total DPSC mission. For these reasons the exchange alternative is less desirable at this time than central management within the Services.

f. Alternative 3 (Joint Service Commissary Agency). The cost analysis of all alternatives contained in Appendix 12-A, Volume II, indicates this alternative provides the greatest overall cost reductions and customer savings. It would also require a minimum lead time of 3 to 5 years. A major deterrent to immediate implementation is the lack of an existing automated management and information system. This alternative is, therefore, not obtainable within the time frame imposed by Program Budget Decision 282. The uncertainties of future sales, savings, and the allocation and assessment of costs also suggest prudence. Based on these uncertainties, it seems inappropriate to recommend future adoption of this alternative at this time.

g. Alternative 4 (Government Owned, Contractor Operated) results in significantly lower savings than any other alternative and is, therefore, impracticable.

2-7. RECOMMENDATIONS.

a. Each military Service should adopt centralized management of its commissary stores.

b. Concurrently, the military Services should develop necessary commissary accounting and ADP systems. The early establishment of a joint-Service committee may be desirable to promote standardization to the extent feasible.

c. Enabling legislation be enacted to:

(1) Delete the requirement that Army and Air Force commissary stores sell each item at invoice cost to permit variable pricing.

(2) Permit funds generated from adjustments of, or surcharge on, selling prices in commissary stores to be invested.

(3) Delete the last sentence of Section 814 of the Defense Appropriations Act which establishes availability, distance, and price criteria for certification of commissary stores.

(4) Add a clause to paragraph 501b of the Defense Appropriations Act excluding commissary employees from end-strength restrictions on civilian personnel to provide flexibility in use of other than full-time employees.

d. The Civil Service Commission be requested by the Department of Defense to provide special recruiting support for employment of a greater number of other than full-time employees.

e. The Services should develop programs to communicate relevant commissary operating and savings information to authorized customers.

f. The resale and troop issue functions should be separated and all support provided by one entity (resale or troop issue) for the other be on a fully reimbursable basis.

g. Effective training programs should be developed to enhance job efficiency in the various commissary functional areas.

h. After the Services have separately adopted centralized management and have been operational for a sufficient period of time to evaluate customer losses and operational costs, the Services should assess whether consolidation into a joint-service commissary system would be cost advantageous to the customers. Such assessment should also focus on the desirability of lesser consolidation such as an Army/Air Force commissary system.

2-8. REVIEW BY SERVICES. The draft report was submitted to each of the Services for their review and comment. The Departments of the Army and Air Force essentially concurred with the conclusion and recommendations in the report. The Department of the Navy felt that Alternative 2, Merger with the Exchange System, was particularly feasible for the Navy and that the Marine Corps commissary system in its present configuration, with possible complexing and other economies through parent and branch store alignments, was most suitable. Appropriate detailed comments and suggestions received from the Services have been incorporated into the final report. Such actions and discussion where appropriate are included in Chapter 13.

CHAPTER 3

SAVINGS PROVIDED BY THE MILITARY COMMISSARY STORE AND ITS RELATIONSHIP TO SALES

3-1. INTRODUCTION. The paramount aspect of the current military commissary store system is the significant savings it provides to the authorized patron. Assessment of the actual savings and the perceived savings is critical to the study due to the impact on sales that a reduction of savings may have. This chapter discusses both the actual and the perceived savings and the projected impact on sales.

3-2. ACTUAL SAVINGS.

a. Recurring provisions of the annual Department of Defense Appropriations Act, currently Section 814, provide:

"That no appropriation contained in this Act shall be available in connection with the operation of commissary stores within the continental United States unless the Secretary of Defense has certified that items normally procured from commissary stores are not otherwise available at a reasonable distance and a reasonable price in satisfactory quality and quantity to the military and civilian employees of the Department of Defense."

b. Implementation of this requirement is accomplished by means of a triennial survey of all commissaries within the United States. The most recent triennial survey conducted in 1972 revealed average savings, as compared to commercial supermarket prices, to be about 24.25 percent (a price differential of 32 percent - state sales taxes applicable to supermarkets and surcharge/markups applicable to commissaries are excluded). The survey consists of a market basket of 89 food items which are weighted to correspond to a family's food buying practices. Items on sale in both supermarkets and commissaries (voluntary price reduction items), and commissary specification items, which are somewhat equivalent to supermarket house brands, are also excluded.

c. Since the fall of 1972, the Navy Resale Systems Office has been conducting semi-annual price comparison surveys in Navy commissary stores. Thirteen CONUS Navy commissary stores in different geographical areas are surveyed each time. The number

of different items priced by each store total 100 and include 86 of the 89 market basket food products plus 14 additional items. Prices are recorded for identical items and include specials and promotions offered by commercial supermarkets. State and local retail sales taxes, where applicable, are not included in commercial prices reported.

(1) A summary of percent savings in CONUS Navy commissary stores when compared to average commercial supermarket prices for the same item is given in Table 1.

Table 1

NAVY COMMISSARY STORE
PERCENT SAVINGS *

Department	Fall '72	Spring '73	Fall '73	Spring '74	Fall '74
All					
departments	21.5	21.0	20.6	21.3	22.0
Range all	16.9 to	15.8 to	16.1 to	18.2 to	16.4 to
departments	26.0	27.6	24.1	25.2	24.6
Groceries	20.8	21.1	20.5	20.7	20.8
Meat	20.2	17.0	18.0	20.5	22.4
Produce	31.2	27.8	27.8	27.6	33.1

*Commissary mark-ons considered.

(2) A review of the above data indicates that actual average savings on identical items range from 20.6 to 22.0 percent over purchasing these items in commercial supermarkets. Individual store average savings ranged from a low of 15.8 percent to a high of 27.6 percent.

d. In December 1974, the Air Force conducted a price survey at 19 bases to determine the current price differential between commercial facilities and commissary stores. The overall price differential was 32.1 percent. After application of a three percent surcharge and conversion of the differential to a percent savings, the patrons were realizing approximately 22 percent savings. Individual store average savings ranged from a low of 17.9 percent to a high of 24.7 percent. The Air Force average and range of savings fall within the range of savings determined by the Navy survey.

e. At the request of the study group a special price comparison survey was conducted in March 1975 for 10 Army commissaries. It included the food market basket of 89 items as well as 14 non-food items. The food and non-food categories were appropriately weighted based on sales importance. A net

savings of 22.38 percent, surcharge considered, was determined. Table 2 reveals the results of the survey, excluding surcharge and sales taxes.

Table 2
MARCH 1975 PERCENT SAVING
ARMY SURVEY RESULTS

<u>Category</u>	<u>Percent Savings</u>
Food plus non-foods	24.55
Foods only	23.35
Non-food only	29.81

f. It can be reliably assumed that the savings shown by the Navy, Air Force and the most recent March 1975 Army survey are representative of the current savings in military commissary stores in the United States. Therefore, the actual average savings to the commissary store customer is between 20.0 and 22.4 percent. These savings do not include any savings that may be realized as a result of not having to pay state and/or local sales taxes. However, some of these additional savings are offset by patrons tipping the personnel who bag the groceries (whose only recompense derives from such source).

g. Since the military price comparison surveys are made by comparing national brand merchandise, the savings figure of 22 percent has been challenged in some quarters. The rationale is that the commissary store patron could buy commercial house brand merchandise rather than national brands at a much reduced price. It is also contended that specials and loss leaders are not taken into consideration. Thus, the rationale continues, the real savings in military commissary stores is between 15 and 17 percent.

h. It is the contention of the study group that the savings range of 20.0 - 22.0 percent as an upper limit, is indeed valid because of the following reasons:

(1) The less expensive house brand merchandise in the civilian sector is offset by troop issue or low price line merchandise that is also carried in most military commissary stores;

(2) The previously mentioned Navy price comparison surveys do take into account special and loss leaders. In addition, the Air Force survey did not include non-food items; and as shown in the March 1975 Army survey, inclusion of non-food items in the survey would increase the percent savings; and

(3) An additional special survey, requested by the study group, was accomplished matching a discount supermarket against a commissary. Items on "sale" and low price items were allowed for the discount supermarket while troop issue or specification items were not allowed in the commissary selection. Results of this survey indicated a 20.5 percent savings in the commissary.

3-3. PERCEIVED SAVINGS.

a. Actual savings are important but perceived savings are what people make their decisions on. In January 1975, the Army conducted a study of approximately 20,000 people. Through a series of questions the Army was able to determine, first, perceived savings and second, what the commissary store patron would do if savings were reduced by a certain percentage. The results of the Army survey in these two areas are in Tables 3 and 4.

Table 3

ARMY PERCEIVED SAVINGS

	<u>Total World-wide</u>	
	<u>Off</u>	<u>EM</u>
Commissary prices are higher than supermarket prices	1.6%	2.3%
Commissary and supermarket prices are about the same	11.4	19.3
Commissary prices are lower than supermarket prices by		
1-5%	21.9	27.8
5-10%	28.0	24.9
10-15%	19.8	12.5
15-20%	10.8	6.7
20-25%	4.1	3.5
25-30%	1.8	1.7

Table 3 (Continued)

	<u>Total World-wide</u>	
	<u>Off</u>	<u>EM</u>
More than 30%	.6	1.3
Sample size	3852	16362

Table 4

CUSTOMER REACTION TO REDUCED SAVINGS

	<u>Total World-wide</u>	
	<u>Off</u>	<u>EM</u>
Don't use the commissary	7.2%	13.5%
I would stop shopping in the commissary if commissary prices as compared to supermarket prices were:		
Same as in the supermarket	50.3	48.9
1-7% lower	21.9	16.3
8-12% lower	8.4	6.8
13-17% lower	2.5	2.8
18-24% lower	1.4	1.5
25-30% lower	1.3	1.3
I will continue to shop in the commissary regardless of price	7.0	8.9
Sample size	3873	16616

b. The Control Analysis Corporation (CAC), Palo Alto, California, conducted a similar study for the Navy. CAC surveyed 64,298 commissary store patrons. One aspect of the study was to determine perceived savings. Table 5 summarizes these results:

Table 5

NAVY PERCEIVED SAVINGS

<u>Perceived Savings</u>	<u>Overall Average</u>	
	<u>% Patrons</u>	<u>% Sales</u>
Less than 10%	19.6	18.5
11-15%	16.6	16.5
16-20%	21.9	22.0
21-25%	16.0	16.3
26-30%	8.3	8.8
31-35%	2.4	2.7
36-40%	2.0	2.1
Over 40%	2.4	2.5
No response	10.4	10.7

c. A third source for data on perceived savings was the 1973 DOD Personnel Survey (Report MR 7411) sponsored by the Office of Assistant Secretary of Defense, Manpower and Reserve Affairs, Directorate for Manpower Systems Evaluations. Results of this survey are depicted in Table 6.

Table 6

DOD PERCEIVED SAVINGS

<u>Perceived Savings</u>	<u>Total World-wide</u>	
	<u>Off</u>	<u>EM</u>
0%	3.2	10.6
1-8.3%	23.9	25.1
8.4-18.0%	36.4	28.9
18.1-22.5%	22.7	18.7
22.6-28.1%	9.1	7.9
28.2-32.9%	2.5	3.7
33-37.1%	1.1	2.4

Table 6 (Continued)

<u>Perceived Savings</u>	<u>Total World-wide</u>	
	<u>Off</u>	<u>EM</u>
More than 37.1%	1.1	2.7
Sample size	13,160	16,950

d. The conclusion that is drawn from a review of the perceived savings is that many commissary store patrons perceive that the savings achieved by buying in military commissary stores are less than they actually are. For example, the surveys showed that between 61.3 and 72.0% of Army personnel perceive savings to be less than 10 percent, 19.6% of Navy customers perceive less than 10 percent savings, while 27.1% to 35.6% of the persons surveyed by DOD perceive savings to be less than the 10 percent figure. Therefore, reducing savings by 10% could mean that these customers would be indifferent to shopping in military commissary stores, causing a significant loss in sales. As commissary stores become self-supporting, military personnel will have to be kept informed concerning the actual savings.

3-4. RELATIONSHIP BETWEEN SAVINGS AND SALES.

a. Using the data from the three surveys, mathematical models were developed for use in projecting lost sales as a result of reduced savings in the commissary stores. Appendix 3A, Figure 1 (Page 3-12) is a graphical display of acquired results. One anomaly revealed by the uppermost curve, as well as Table 3, above, is that Army personnel perceive commissary savings to be much less than they actually are. Whereas, when the same Army personnel were asked what they would do if savings were reduced by a given percentage, the responses (Table 4) were more in line with Navy results. It appears appropriate for all services to undertake a campaign to educate personnel as to the "true" worth of the commissary store benefit.

b. The exponential equations for the three curves in Appendix 3A, Figure 1 (Page 3-12), yield Table 7 (Page 3-8).

Table 7

FORECASTED LOST SALES
BASED ON PERSONNEL SURVEYS

Percent Savings %	Forecasted % Lost Sales		Percent Savings %	Forecasted % Lost Sales	
	Army/Navy Survey	DOD Survey		Army/Navy Survey	DOD Survey
1	64.5	63.3	12	13.1	23.9
2	55.8	57.3	13	11.3	21.9
3	48.2	52.5	14	9.8	20.1
4	41.7	48.1	15	8.5	18.4
5	36.1	44.1	16	7.3	16.9
6	31.2	40.4	17	6.3	15.4
7	27.0	37.0	18	5.5	14.1
8	23.3	33.9	19	4.7	13.0
9	20.2	31.1	20	4.1	11.9
10	17.5	28.5	21	3.5	10.9
11	15.1	26.1	22	3.1	10.0

c. The Army and Navy data were combined into a single curve and compared to the DOD survey based curve. This table of forecasted loss of sales as a function of savings was used to determine the impact on sales as the study group assessed the various alternatives under consideration. Table 7 reveals that the DOD curve projects greater lost sales for the same percent savings than the combined Army/Navy curve. For example, a savings of 10 percent produces a 17.5 percent loss of sales using the Army/Navy curve and a 28.5 percent loss of sales using the DOD curve. It is believed that this is due to the following reasons:

(1) The difference in the "wording" of the questions. Army and Navy questions used a percent figure, whereas the DOD questions were based on dollar amounts.

(2) The DOD survey was taken in October 1973 versus the Navy and Army surveys which were accomplished in July 1974 and January 1975, respectively. The difference in time and inflation rates of the U.S. economy, in general, could have affected the perceptions of commissary customers. The DOD curve which was based on an older survey, revealed greater lost sales.

(3) However, more important is the fact that the Army and Navy surveys allowed for identification and elimination of responses for those individuals who stated non-use of the commissary. Unfortunately, the DOD survey did not allow for this action to be taken and, thus, included in the sample are the responses of individuals not using the commissary which could bias the results of the survey.

d. For the purpose of the study it was decided to assess each of the operating alternatives using a range of possible "lost sales." The Army/Navy results were, therefore, used as the lower limit whereas the DOD based results were used as the upper limit. It is recognized that a very important assumption has been made, i.e., the derived relationship between lost sales and percent savings is indeed valid and, more crucial yet, that this relationship will continue under any proposed change to the commissary system. In view of the strong statistical findings discussed in Appendix 3A, and the uncertainty that is unavoidable when restructuring any system, the models were deemed to be acceptable. However, it cannot be overemphasized that, although the study group believes that the two lower curves represent the "most likely" outcomes, it is possible that without a strong education and/or public information program as to actual savings, lost sales could assume the proportions depicted by the Army Perceptions Based Curve. If this were to occur, there is the possibility that the commissary system could lose up to 43 percent of its sales by the end of FY 1976. It would be

extremely difficult to cope with the follow-on consequences of such a sales loss.

3-5. APPLICATION OF LOST SALES/PERCENT SAVINGS RELATIONSHIPS.

a. Using computer simulation techniques, each of the proposed alternatives for commissary operations was tested for its effect on the level of savings and impact on sales. It has been stated that, as savings are reduced, patronage should decline causing increasing losses in sales. However, in the short run, it is very unlikely that reduced sales will allow an equal amount of reductions in costs. Therefore, the fixed portion of costs will have to be pro-rated among the lower sales volume causing even greater losses in savings. In order to determine which of the various operating alternatives best coped with this effect, the Lost Sales/Percent Savings model discussed in paragraph 3-4, was incorporated into a cost analysis model which first, matched costs to revenues (sales); second, produced a percent savings; and third, projected any expected lost sales, and their impact on prior findings.

b. Appendix 3-C is a description of the cost analysis model. Output of this model for each of the studied alternatives has been used as the primary tool for the study group's economic analysis. These results are included in Chapters 4 and 6 through 9.

APPENDIX 3-A

SALES/SAVING RELATIONSHIP

3-A.1 PURPOSE. This appendix describes the relationship between savings incurred by commissary patrons and lost sales. It also provides an explanation of the methodology used in developing estimates of this relationship.

3-A.2 DESCRIPTION OF RELATIONSHIP.

a. Figure 1, page 3-12, is a graphical display of the relationship of lost sales to customer savings. The vertical axis is lost sales in percent, whereas, savings as a percent of sales is on the horizontal axis. The three curves shown in the graph reveal that as percent savings decline, losses in sales increase at an exponential or accelerating rate. The difference between the three curves is due to the use of independent sources of data in their derivation.

b. The top curve (labeled Army Perceptions) is based on a series of questions from a January 1975 Army survey which asked military personnel to compare commissary prices to commercial supermarket prices. Their responses indicate that Army personnel perceive commissary savings to be much less than actual savings.

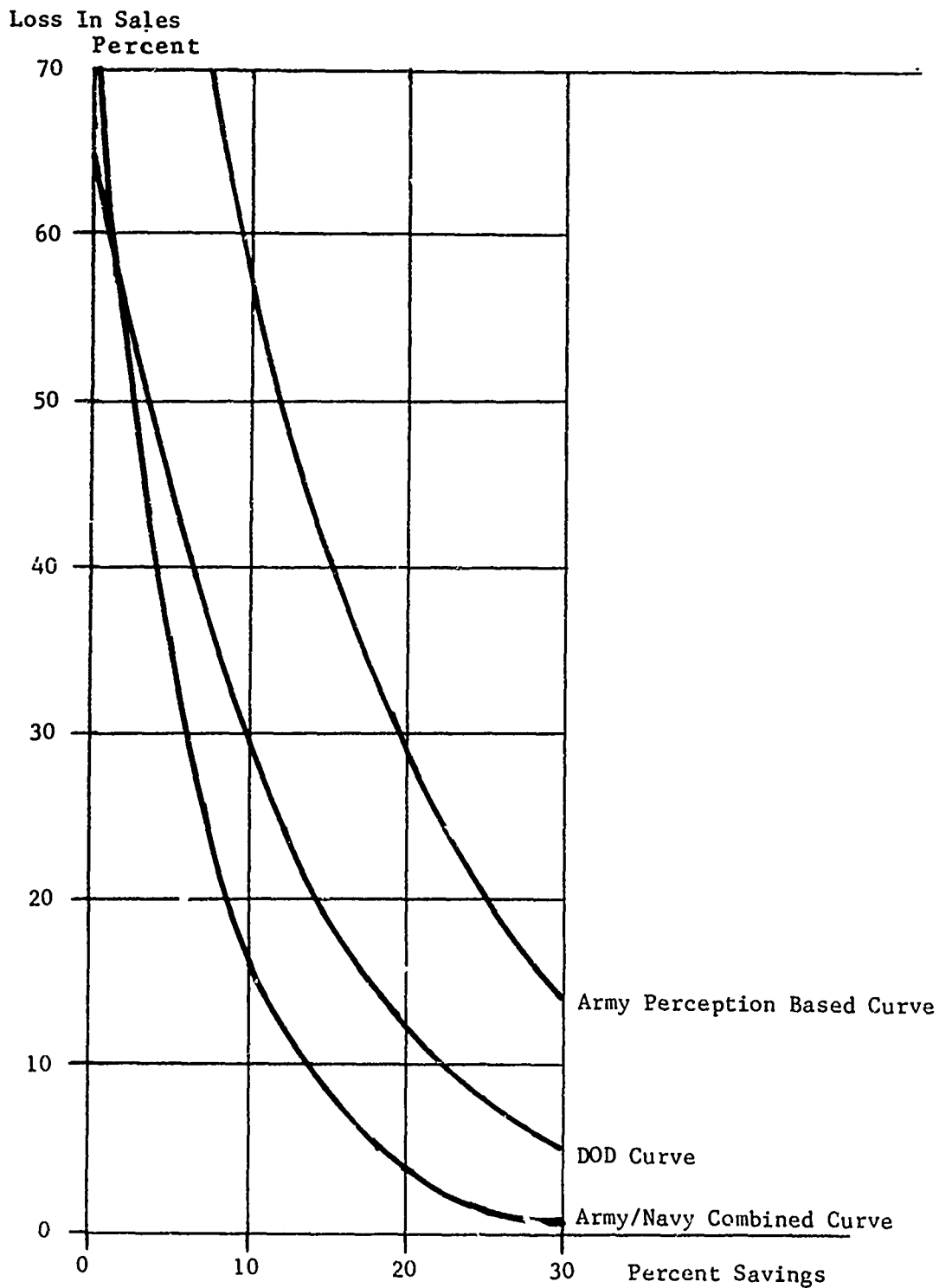
c. The lower curve (labeled Army/Navy Combined Curve) was derived using responses to a second series of questions from the January 1975 Army survey and a survey performed for the Navy by the Control Analysis Corporation. It is interesting to note that, when Army personnel were asked at what percent savings would they cease to shop at the commissary, their responses (intentions) produced a lost sales/percent savings relationship much more in line with other service personnel.

d. The middle curve is based on a series of questions in the Quadrennial Department of Defense Personnel Survey of 1973. Although it produces higher estimates than the combined Army/Navy curve, it is still considerably lower than the curve based on Army "perception" data (top-most curve).

3-A.3. METHODOLOGY USED FOR ESTIMATING RELATIONSHIPS.

a. Survey questions and responses used for developing the three curves are given in Chapter 3, Tables 3 through 6. Cumulative distributions of the responses were calculated for each of the surveys and regression analysis was used to develop the curves. Percent savings were treated as the independent variable and lost sales percent as the dependent variable. Original values of lost sales for input into the regression

FIGURE 1
LOSS IN SALES PERCENT VS PERCENT SAVINGS



analysis program were calculated as in the following example:

(1). If 19.6 percent of personnel surveyed responded that they perceived savings to be less than 10 percent, and if these personnel accounted for 18.5 percent of the commissary sales, then it was assumed that, when actual savings decreased from 22 percent to 12 percent (a 10 percentage points difference), an 18.5 percent loss in sales would be generated since those people perceiving their savings as only 10 percent would cease to shop in the commissaries.

<u>Perceived Savings</u>	<u>Actual Savings</u>	<u>Actual Savings Decline to</u>	<u>Lost Sales</u>
Less than 10 percent	22 percent	12 percent	18.5 percent

(2). Now, assume that a second group of personnel, representing 16.5 percent of sales, perceive savings to be between 11 and 15 percent. Then, when actual savings decline further from 12 percent to 7 percent (the 5 percentage points difference between first group's perceptions and second group's perception, one can expect another 16.5 percent loss in sales for a total of 35 percent lost sales.

<u>Perceived Savings</u>	<u>Actual Savings</u>	<u>Actual Savings Decline to</u>	<u>Lost Sales</u>
Less than 10 percent	22 percent	12 percent	18.5 percent
11-15 percent	12 percent	7 percent	18.5+16.5=35 percent

b. This process was accomplished for the three surveys. The results were then subjected to regression analysis and the equations for the curves developed. Table 1 below is a summary of the equations and statistical findings for each of the three curves:

TABLE 1
LOSS SALES/SAVINGS
STATISTICAL FINDINGS

CURVE LABEL	TYPE OF CURVE	EQUATION CONSTANTS	COEFFICIENTS OF CORRELATION DETERMINATION*	
1. Army Perception	Exponential $Y=ae^{bx}$	$a=120.251$ $b=-.072014$	-.935	.874
2. ARMY/NAVY Based	" "	$a=74.579$ $b=-.1451683$	-.954	.910
3. DOD Based	" "	$a=68.271$ $b=-.087445$	-.952	.906

*The coefficient of determination indicates what percent of the variation in lost sales is explained by the variations in savings. For example, using the Army/Navy based curve, 91 percent of the variations in lost sales is determined by savings to the customer and approximately 9 percent is determined by unexplainable factors. A test of significance for the coefficient of determination produces a statistic "t" value of 7.79 which exceeds the "t" value at a .001 level of significance.

c. All three curves are of the exponential form $Y = ae^{bx}$ where

Y = Loss Sales

a = Equation Constant

e = The Natural Number 2.7183

x = Percent Savings

b = Equation Constant

d. Appendix 3-B contains tabular results for each curve including a 95 percent confidence interval for the average percent of lost sales given various levels of percent savings.

APPENDIX 3-B

FORECASTED LOST SALES

95 PERCENT CONFIDENCE INTERVALS

TABLE 1

ARMY/NAVY CURVE

Percent Savings	Forecasted % Lost Sales	95% Confidence % Lost Sales	Percent Savings	Forecasted % Lost Sales	95% Confidence % Lost Sales
1	64.5	61.8-67.2	12	13.1	10.4-15.7
2	55.8	53.1-58.5	13	11.3	8.6-14.0
3	48.2	45.6-50.9	14	9.8	7.0-12.5
4	41.7	39.1-44.4	15	8.5	5.7-11.2
5	36.1	33.5-38.7	16	7.3	4.5-10.1
6	31.2	28.6-33.8	17	6.3	3.4-9.2
7	27.0	24.4-29.6	18	5.5	2.5-8.4
8	23.3	20.8-25.9	19	4.7	1.7-7.7
9	20.2	17.6-22.8	20	4.1	1.0-7.2
10	17.5	14.9-20.1	21	3.5	.4- 6.7
11	15.1	12.5-17.7	22	3.1	.0- 6.3

TABLE 2

DOD CURVE

Percent Savings	Forecasted % Lost Sales	95% Confidence % Lost Sales	Percent Savings	Forecasted % Lost Sales	95% Confidence % Lost Sales
1	62.6	55.4-69.7	12	23.9	17.9-29.9
2	57.3	50.3-64.3	13	21.9	16.0-27.8
3	52.5	45.7-59.4	14	20.1	14.2-26.0
4	48.1	41.4-54.8	15	18.4	12.5-24.3
5	44.1	37.5-50.6	16	16.9	10.9-22.8
6	40.4	33.4-46.8	17	15.4	9.5-21.4
7	37.0	30.7-43.4	18	14.1	8.2-20.1
8	33.9	27.7-40.2	19	13.0	6.5-19.0
9	31.1	24.9-37.2	20	11.9	5.8-18.0
10	28.5	22.4-34.6	21	10.9	4.7-17.0
11	26.1	20.1-32.1	22	10.0	3.7-16.2

TABLE 3

ARMY PERCEPTIONS CURVE

Percent Savings	Forecasted % Lost Sales	95% Confidence % Lost Sales	Percent Savings	Forecasted % Lost Sales	95% Confidence % Lost Sales
1	100	—	12	50.7	39.4-62.0
2	100	93.0-100	13	47.2	36.1-58.2
3	96.9	79.8-100	14	43.9	33.0-54.7
4	90.2	73.9-100	15	40.8	30.0-51.6
5	83.9	68.4-99.3	16	38.0	27.1-48.8
6	78.6	63.4-92.7	17	35.4	24.3-46.4
7	72.6	58.7-86.6	18	32.9	21.6-44.2
8	67.6	54.3-80.8	19	30.6	18.9-42.3
9	62.9	50.2-75.6	20	28.5	16.4-40.6
10	58.5	46.4-70.7	21	26.5	13.8-37.2
11	54.5	42.8-66.1	22	24.7	11.4-37.9

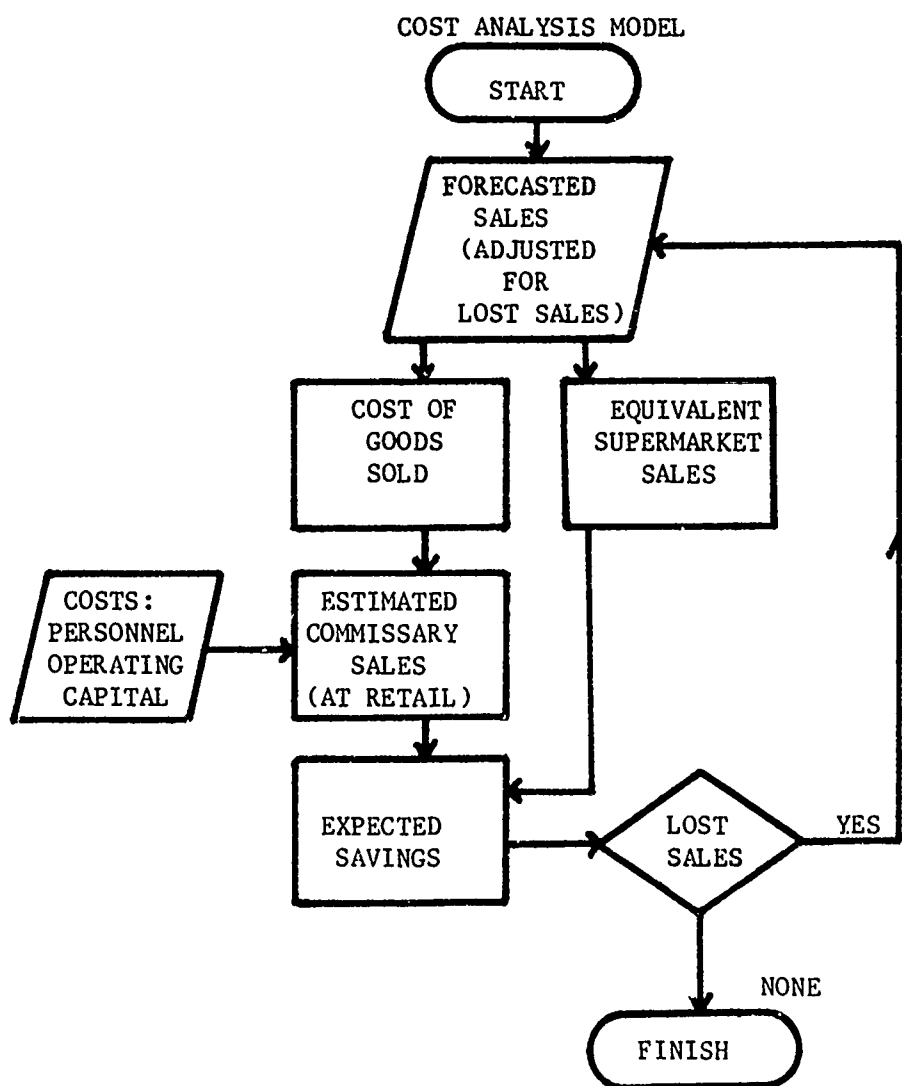
APPENDIX 3-C

DESCRIPTION OF COST ANALYSIS MODEL

3-1. DESCRIPTION OF THE MODEL.

a. Because of the interwoven relationships between costs, savings, and sales volumes, it was determined that a simulation type model had to be constructed which could be used as an aid in performing the quantifiable portion of the Study Group's economic analysis. The model had to consider not only the affect of changes in costs on savings, but also how these results would be in turn affected by consequential changes in sales volumes. Figure 1 is a display of the developed model.

FIGURE 1



b. Although this was a simplified approach to a very complex problem, it did incorporate all the vital ingredients. The model allowed for determination of the four basic cost factors: cost of goods sold, personnel, operating expenses, and capital; and used these cost factors to establish commissary retail sales, the equivalent commercial supermarket sales, and savings to the patron. It then applied the lost sales/percent savings relationship described in Appendix 3-A to determine the amount of lost sales generated by the reduced savings, as well as the subsequent effect of the reduced sales level. In effect the model provides a realistic, although somewhat simplified, solution to the problem of uncertainty confronting the study group.

3-2. ASSUMPTIONS

a. That the actual savings to commissary patrons is currently about 22 percent.

b. That the existing relationship between supermarket prices and commissary cost of goods sold will remain constant.

c. That the current commissary markup relationship between CONUS and overseas locations will continue.

d. That the lost sales/percent savings relationship established in Appendix 3-A is valid. This implies that an effective information program will be implemented to change the patrons' perceptions of savings so that perceptions will correspond to actual savings.

e. That real growth does not apply. Historically, the commissary system has realized a 2.0 to 2.9 percent real growth factor. However, the study group has taken a conservative approach and does not consider this factor in its calculations.

f. That an 80/20 percent fixed/variable relationship is applicable for operating expenses. The model maintained 80 percent of the operating expenses as fixed, as sales decreased during the year. A more liberal 50/50 relationship was allowed for the commercial contract analysis.

g. That the commissary patron is a rational economic man, that he will switch to the civilian market as savings decline in the commissary, and that he will do this according to the perceptions and intentions revealed in the previously described surveys.

h. That once a customer stops to shop in the commissary, he does not return to it. Although there is a possibility that some customers will return, there is no basis available for quantifying this factor and incorporating it into the model.

3-3. METHODOLOGY

a. FY 76 estimated sales, as projected under the current operating systems, were used as the base figures in forecasting sales for each of the alternatives.

b. Expenses for the period 1 October 1975 to 30 September 1976 (3/4 of FY 76 and FY 77) were 100 percent of the projected operating expenses and capital outlays, and 50 percent of the direct personnel and overseas utility expenses (as required by PBD 282). A deviation from this practice was allowed for alternative #2 (Merger with Exchange Services) in that it was assumed that the Army and Air Force Exchange Service (AAFES) would operate the Army and Air Force Commissaries for 180 days and the services would operate them for 180 days. Therefore, expenses for this alternative for the period 1 October 1975 to 30 September 1976, were based on 50 percent of AAFES and 50 percent of Army/Air Force costs.

c. Total expenses were then added to cost of goods sold to achieve the estimated commissary sales. This retail figure was subtracted from the equivalent supermarket sales figure (based on the original forecasted commissary sales) and a savings determined. The savings, as percent of equivalent supermarket sales, were then introduced into the subordinate lost sales/percent savings model to determine the percent of lost sales generated. This loss of sales would require a higher markup to cover expenses because of fixed costs and the resulting decrease in the base sales figure. Reducing sales each time the markup was increased and increasing the markup to cover expenses was continued until the incremental sales lost were less than 0.01 percent, a figure considered too small to require any further adjustment to markup.

d. The resultant net sales for the 1 October 1975 to 30 September 1976 period were then used as the forecasted sales for FY 77. Expenses for FY 77 were 100 percent of all direct costs, operating expenses, and capital outlay. The same process was applied, by the model, for fiscal years 1977 and 1978. For most alternatives the model revealed no additional increase in the markup for FY 1978, and thus no further reduction in patronage.

CHAPTER 4

PRESENT SERVICE COMMISSARY SYSTEMS

4-1. GENERAL.

a. The existing commissary systems of the military services are similar but they include several distinct differences. This chapter will summarize each of the present systems and address the similarities and differences of the systems. Military commissaries are operated pursuant to the laws cited in Chapter 11, the annual Department of Defense Appropriations Acts and Department of Defense Directive Number 1330.17, dated 29 October 1971, as changed, subject: Armed Services Commissary Store Regulations. The Department of Defense prescribes broad commissary policy. Detailed policies and operating procedures are established by each of the military services. A detailed description of the commissary system used by each service is provided at Chapter 4, Volume II.

b. Figures 1 and 2 (Pages 4-8 and 4-9) provide general statistical information regarding the operations of the military service commissary systems during Fiscal Year 1974. These figures show the scope of the military commissary store programs, those operating costs which were financed with appropriated funds, and those costs for which reimbursement was effected. Using this data, Figures 3 and 4 (pp 4-10 and 4-11) were developed to show the economic impact of PBD 282 on the present Service commissary store systems. These figures show that the expected customer savings percent will range from 11.2% to 14% and the expected sales loss will range from 9.7% to 25.6%.

c. Each of the military services has developed a commissary reporting system which provides certain operational data for management purposes. Four basic measures of productivity used by all services are shown at Figure 5 (Page 4-12) and are compared with similar data for commercial supermarkets. To obtain a realistic comparison, commissary sales figures were adjusted to reflect the average differential between commissary and commercial prices. The results of this comparison are favorable to the military commissaries but they reflect, also, the general inadequacy of facilities and customer service according to commercial standards.

4-2. THE ARMY COMMISSARY SYSTEM.

a. Army commissaries operate on a decentralized basis. Each store is operated independently and control is exercised through command channels (Figure 1, APPN 4-A, Vol II). Broad policy is supplemented by the Deputy Chief of Staff for Logistics, Department of the Army and technical guidance is provided by the U. S. Army Troop Support Agency, an operational element of the DCSLOG, DA. Army commissary officers are responsible for troop issue subsistence and commissary store operations.

b. Subsistence inventories are procured with Army Stock Funds.

Reimbursement for commissary store subsistence is made from cash sales and for troop issue subsistence by direct charge to the Military Personnel, Army, appropriation. Appropriated funds are used to finance the salaries of commissary store military and civilian personnel and other operational costs. Surcharge funds, which accrue from collection of a surcharge on commissary store sales, (3% in CONUS and Hawaii, 2 1/2% overseas including Alaska), are used to reimburse appropriated funds for the costs of supplies, equipment, equipment maintenance, utilities (U.S. excluding overseas and Alaska), laundry, telephone, losses and construction - alteration projects not financed with appropriated funds. Military Construction, (MILCON), funds are used to finance major construction projects for overseas commissaries.

c. In the United States, commissary officers order the majority of their subsistence requirements under contracts awarded by the Defense Personnel Support Center (DPSC). Local purchase is optional for fresh fruits and vegetables and is authorized for brands not listed in DPSC contracts. Overseas, commissary officers order from DPSC through the U.S. Army Materiel Management Agency Europe (USAMMAE). DPSC consolidates requirements and orders from suppliers in the United States. Offshore procurement is used for certain highly perishable items such as fresh fruits and vegetables and carcass beef for Europe. Commissary officers verify invoices for payment by installation finance and accounting officers.

d. The product groups which may be stocked in Army commissaries are restricted to those specified in DA Supply Bulletin 10-512. In the U.S., the selection of individual items, brands and sizes within those product groups is determined by each commissary officer. Overseas, stockage of specific items for all commissaries is prescribed with local choice authorized as a percentage of the total number of items stocked. The Army operates no distribution centers or central meat processing centers for commissaries.

e. Army commissary stores and warehouses are generally inadequate. Most facilities are congested, inefficient, unattractive to customers, and were designed for other purposes. Recent efforts to improve these facilities have resulted in the construction of eight new commissary stores using both appropriated funds and residual surcharge funds for construction and new equipment. Additional requirements for new construction and equipment are estimated at \$172.1 million. The Army is developing standard designs, layouts, and equipment lists for new commissaries to achieve economies in design and construction costs. New and replacement equipment requirements of each commissary are procured with surcharge funds as part of the annual surcharge budget.

4-3. THE NAVY COMMISSARY SYSTEM.

a. Navy commissaries operate under a centralized concept with command and control exercised by the Navy Resale Systems Office (NRSO) (Figure 1), APPN 4-B, Vol II). NRSO provides direct technical management and financial control. Host commands where stores are located provide certain administrative services and utilities support. Navy has grouped commissaries geographically by establishing complexes which provide centralized administration, procurement, accounting, and ADP support for the individual stores in each complex. Navy commissaries have no responsibility for the troop issue function except in Taiwan.

b. Resale stocks are procured with Navy Stock Funds which are reimbursed from the proceeds of commissary store sales. Salaries of military and civilian commissary store personnel are paid from appropriated funds. Selling prices of individual items are marked up approximately 5% to reimburse appropriated funds for prescribed costs of operation. Excess collections are used to finance construction and improvement projects. MILCON funds are used to pay for construction of commissaries at overseas bases, and in remote areas of the United States.

c. The majority of items required for resale are obtained from suppliers under DPSC contracts. Local procurement is used for some items and is optional for fresh fruits and vegetables. Invoices are reconciled at the complexes for payment by Regional Finance Centers.

d. NRSO specifies the broad product group limitations for commissary stockage. A selection board at each complex determines the individual items to be stocked and to be discontinued at each store within the complex. Tobacco products, soft drinks and candy are not sold in Navy commissaries. Central warehousing is in effect at 10 complexes. One central meat processing center is in operation and two more are being constructed.

e. Most Navy commissaries are housed in inadequate facilities which are not conducive to supermarket type operations. The cost of construction and improvement of commissary facilities and replacement of equipment is estimated at \$171.1 million. During recent years, funds have been appropriated for the construction of only one new commissary store, (Adak, Alaska).

4-4. MARINE CORPS COMMISSARY SYSTEM.

a. Commissary operations in the Marine Corps are decentralized. Each commissary is independent and operates under normal command channels (Figure 1, APPN 4-C, Vol II). The Deputy Chief of Staff for Installations and Logistics, Marine Corps Headquarters, has staff responsibility for commissaries while installation commanders have operational control of their commissary stores. Marine Corps commissaries have no responsibility for the troop issue function.

b. Merchandise for resale is procured with Marine Corps Stock Funds which are reimbursed from cash sales in commissary stores. Appropriated funds finance military and civilian salaries, travel and building maintenance costs. The prescribed operating expenses are paid from an average markup of from three to five percent over the cost of goods which is added to the selling price of each item. Revenue from markups is also used to pay for the purchase of capital assets and commissary store improvements.

c. Resale merchandise is procured from suppliers under DPSC contracts and under local purchase procedures. Invoices are verified by commissary officers and paid by installation disbursing officers.

d. Marine Corps commissary stockage categories parallel those of the Navy except that soft drinks and candy are included. Maximum stockage limits are not prescribed and item selection is determined by each commissary officer. No centralized storage or processing centers are operated.

e. Commissary store facilities have been improved with surcharge funds. One new commissary store has been built and two are under construction. The long range improvement program for commissary facilities is estimated at \$10 million.

4-5. THE AIR FORCE COMMISSARY SYSTEM.

a. Air Force commissary operations are decentralized. Base commanders have control and operational responsibility for their commissaries. They receive policy guidance from Headquarters USAF and the Air Force Logistics Command through major commanders (Figure 1, APPN 4-D, Vol II). Technical assistance is provided by the Air Force Services Office of the Air Force Logistics Command. Each commissary operates independently. Air Force commissary officers are responsible for both troop issue and resale functions.

b. Commissary store inventories are financed with stock funds which are reimbursed from sales receipts. Troop subsistence issues are charged to appropriated funds. Military and civilian personnel costs are paid from appropriated funds. Surcharge collections (3% of sales) are used to reimburse appropriated funds for utilities and to purchase equipment, operating supplies, minor construction projects and equipment maintenance. Commissary construction overseas is financed with MILCON funds.

c. Subsistence items required for troop issue and resale are obtained under contracts awarded by DPSC. Commissary Officers may procure fresh produce and non-brand name items locally. Verified invoices for commissary resale items are forwarded for payment by Base Finance and Accounting Officers.

d. Air Force and Army commissary store stockage categories and item selection policies are generally the same. The number of product groups is controlled but Base commissary officers determine the individual stockage of their stores. There is no restriction on the number of items that may be stocked. There are no distribution centers or central meat processing facilities in operation.

e. The majority of Air Force commissary sales and storage facilities are inadequate, requiring replacement or major renovation to reach acceptable standards. Recent efforts have resulted in some new facilities and improvement of others. Current requirements for new construction - alteration of commissary stores, including equipment, are estimated at \$104 million.

4-6. SIMILARITIES AND DIFFERENCES IN THE MILITARY COMMISSARY SYSTEMS.

a. All of the military commissary systems share the common mission of providing authorized items for sale at the lowest

practicable price. To accomplish this mission there are numerous elements of commissary store management and operational policy in the systems which are identical or similar. In a very broad sense, the Army and the Air Force systems closely parallel each other, while the Navy and the Marine Corps systems are similar in many respects.

b. A partial listing of similar policies in the military commissary systems includes: establishment of commissary policy and provision of technical guidance at the departmental headquarters level; use of stock funds to finance procurement of inventory for resale and procedures for reimbursement of stock funds; use of appropriated funds for military and civilian salaries and related personnel costs; procurement of merchandise for resale from suppliers under contracts awarded by the Defense Personnel Support Center; and the verification and payment of vendor invoices.

c. The following are some of the more important elements of commissary operations and management which differ among the services:

(1) Army, Air Force and Marine Corps commissary operations are decentralized with command and control exercised through normal military channels. The Navy commissary system is centrally managed and controlled.

(2) Navy commissaries are grouped geographically into complexes and each complex has a central office to accomplish administration, procurement and accounting for the stores in the complex. In a similar manner, the Army uses a parent and branch store concept to provide service at nearby installations, with all administration, procurement and accounting being accomplished at the parent commissary. The commissaries of the other services are independent operations, with each commissary having its own administrative office.

(3) In the Army and Air Force, the commissary officers have responsibility for troop issue and resale operations while Navy and Marine Corps commissary officers have no responsibility for troop issue except for the Navy in Taiwan.

(4) Military personnel are utilized at commissary store level to a lesser extent by the Army, Air Force and Marine Corps than by the Navy.

(5) Annual recurring provisions of the DOD Appropriations Act prescribe that certain costs of operating commissary stores must not be paid ultimately by appropriated funds. Although the provisions of this Act are equally applicable to all commissaries, each military service has established different means to pay such costs and reimburse

appropriated funds. The Army and Air Force assess a surcharge at the cash register, based on the total sale. This surcharge rate is 3% in CONUS and Hawaii and 2 1/2% overseas, including Alaska, for the Army and 3% worldwide for the Air Force. The Navy and Marine Corps include a markup in the selling price of each item. The markup varies from 3 to 5%, according to the needs of the particular store.

(6) Each military service used a different procedure to round off fractional unit prices to the next higher or lower cent.

(7) The product groups stocked for resale in each of the service commissaries are the same except that Navy commissaries exclude tobacco, candy and soft drinks while Marine Corps commissaries exclude tobacco products.

(8) The Navy commissary system uses central warehousing and some central meat processing facilities while the other services do not.

FIGURE 1

SCOPE OF MILITARY COMMISSARY STORES PROGRAM

FY 1974
(\$ Millions)

	<u>ARMY</u>	<u>NAVY</u>	<u>MARINE CORPS</u>	<u>AIR FORCE</u>	<u>TOTALS</u>
Sales in U.S.	\$ 719.1	\$ 405.8	\$ 75.7	\$ 930.7	\$ 2131.3
Sales Overseas	\$ 191.8	\$ 58.6	\$ 1.3	\$ 134.3	\$ 386.0
Total Sales <u>1/</u>	\$ 910.9	\$ 464.4	\$ 77.0	\$ 1065.0	\$ 2517.3
Inventory (Average)	\$ 68.9	\$ 34.9	\$ 5.5	\$ 85.6	\$ 196.6
On Order (Average)	\$ 34.5	\$ 18.2	\$ 2.9	\$ 66.7	\$ 122.3
Stock Turn	13.2	13.3	14.1	12.4	12.9 (Average)
Change Fund (Est)	\$ 0.65	\$ 0.60	\$ 0.09	\$ 0.50	\$ 1.84
No. Stores					
In U.S.	73	64	11	132	280
No. Stores Overseas	73	29	1	41	144
Total Stores	146	93	12	173	424
<u>STAFFING</u>					
Above Store Level:					
Military	47	143	0	35	225
Civilian	98	462	2	36	598
Total	145	605	2	71	823
At Store Level:					
Military	226	1020	20	640	1906
Civilian	10,304	3781	825	10,013	24,923
Total	10,530	4801	845	10,653	26,829
Combined Total:					
Military	273	1163	20	675	2131
Civilian	10,402	4243	827	10,049	25,521
Total	10,675	5406	847	10,724	27,652

1. Sales stated at Cost of Goods Sold.

FIGURE 2
DIRECT COSTS OF MILITARY COMMISSARY OPERATIONS
FISCAL YEAR 1974
(\$000)

<u>APPROPRIATED FUND COSTS</u>	<u>ARMY</u>	<u>NAVY</u>	<u>MARINE CORPS</u>	<u>AIR FORCE</u>	<u>TOTAL</u>
Military Personnel	2,716	9,027	309	6,551	13,603
Civilian Personnel	66,874	31,035	8,525	86,255	192,689
Other Purchased Services	18,173			5,163	23,336
Travel	205	80		48	333
Utilities (Overseas Excluding Alaska)	405	960		330	1,695
Other Supplies	293			338	631
Equipment	292			243	535
Military Construction	5,865			7,411	13,276
Sub Totals	\$94,823	\$41,102	\$8,834	\$106,339	\$251,098

SECTION 814 REIMBURSABLE COSTS

Equipment	2,992		2,104	8,242	19,152
Consumable Supplies	7,340		795	8,332	16,467
Dir Dept Expenses		5,814	334		4,210
Equipment Maintenance	3,371	(Note 2)		2,070	5,441
Utilities (U.S. Less Alaska)	1,392	1,938	300	1,970	5,600
Linen Svc/Laundry	172	(Note 2)		634	806
Facilities	6,230	8,990		4,553	19,773
2nd Destination Transp.			184	192	376
Losses (Note 1)	2,904	4,360	611	4	7,879
Sub Totals	\$24,401	\$24,978	\$4,328	\$25,997	\$79,704
TOTALS	\$119,224	\$66,080	\$13,162	\$132,336	\$330,802

NOTES: 1. Since methods of computing losses differ between the services, direct comparisons are not valid.

2. These costs are included with costs for equipment and consumable supplies.

FIGURE 3

ECONOMIC IMPACT AND COST COMPARISON BY MILITARY SERVICE
OF THE PRESENT SERVICE COMMISSARY SYSTEMS

(LOW SALES LOSS - DOD CURVE *)

ITEM		3/4 FY 1976 & 77			FY 1977			FY 1978		
		A	AF	N	A	AF	N	A	AF	N
MILITARY SERVICE										
Assumed Initial Savings	%	22.6	22.0	22.0	17.6	17.5	17.4	13.7	13.5	12.7
Assumed Incremental Sales Loss	%	5.5	5.6	5.5	3.8	4.0	3.9	-	NONE	-
Equivalent Supermarket Sales	\$M	1223.0	1524.7	660.5	1169.9	1455.1	628.7	1183.1	1455.1	628.7
Estimated Commissary Sales	\$M	1007.9	1257.8	546.0	1009.4	1258.2	549.0	1017.2	1256.9	547.9
COSTS:										
Cost of Goods Sold	\$M	925.8	1154.2	488.8	885.6	1101.5	465.3	895.6	1101.5	465.3
Cost of Goods Sold	% Sales	91.9	91.8	89.5	87.7	87.5	84.8	88.0	87.6	84.9
Personnel	\$M	46.2	55.7	27.9	89.8	111.4	56.2	88.1	111.4	56.2
Personnel	% Sales	4.6	4.4	5.1	8.9	8.9	10.2	8.7	8.9	10.3
Operations	\$M	25.8	36.4	19.2	23.9	34.3	17.6	23.3	33.1	16.7
Operations	% Sales	2.6	2.9	3.5	2.4	2.7	3.2	2.3	2.5	3.0
Capital Outlay	\$M	10.1	11.5	10.0	10.1	11.0	10.0	10.2	11.0	10.0
Capital Outlay	% Sales	1.0	.9	1.8	1.0	.9	1.8	1.0	.9	1.8
Total Costs (Less CGS)	\$M	82.1	103.6	57.1	123.8	156.7	83.8	121.6	155.5	82.9
Total Costs (Less CGS)	% Sales	8.1	8.2	10.5	12.3	12.5	15.3	12.0	12.4	15.1
Expected Incremental Sales										
Loss	%	.3	.3	.5	.6	.6	2.0	1.6		.6
Year End Expected Total										
Sales Loss	%	5.8	5.9	6.0	10.2	10.5	11.9	9.7	10.3	11.6
Expected Savings	%	17.6	17.5	17.4	13.7	13.5	12.7	14.0	13.6	12.9

*Derivation of these Curves is discussed in Chapter 3, Volume I.

FIGURE 4

ECONOMIC IMPACT AND COST COMPARISON BY MILITARY SERVICE
OF THE PRESENT SERVICE COMMISSARY SYSTEMS

(HIGH SALES LOSS - DOD CURVE *)

ITEM	3/4 FY 1976 & 77				FY 1977				FY 1978			
	A	AF	N	MC	A	AF	N	MC	A	AF	N	MC
MILITARY SERVICE												
Assumed Initial Savings	22.0	22.0	22.0	22.0	17.0	16.9	16.4	18.2	12.5	12.3	10.9	12.2
Assumed Incremental Sales Loss	14.3	14.4	14.3	14.3	5.9	60.3	7.1	7.1	-	NONE	-	-
Equivalent Supermarket Sales	1099.4	1369.8	590.6	103.8	1019.9	1266.9	532.0	94.3	1019.9	1266.9	532.0	94.3
Estimated Commissary Sales	912.8	1138.7	493.6	85.0	892.0	1110.7	474.3	82.8	889.0	1108.8	472.3	82.5
COSTS:												
Cost of Goods Sold	832.2	1036.9	437.1	76.8	772.0	959.0	393.7	69.8	772.0	959.0	393.7	69.8
Cost of Goods Sold	91.2	91.1	88.6	90.4	86.5	86.3	83.0	84.3	86.8	86.5	83.4	84.6
Personnel	46.2	55.7	27.9	3.8	89.8	111.4	56.2	9.3	88.1	111.4	56.2	9.3
Personnel	5.1	4.9	5.6	4.5	10.1	10.0	11.8	11.2	9.9	10.0	11.9	11.3
Operations	25.3	35.6	18.7	3.4	21.3	30.6	14.4	2.9	20.0	28.8	12.4	2.9
Operations	2.8	3.1	3.8	4.0	2.4	2.8	3.3	3.5	2.2	2.6	2.6	3.3
Capital Outlay	9.1	10.4	10.0	.9	8.9	9.6	10.0	.8	8.9	9.6	10.0	.8
Capital Outlay	1.0	.9	2.0	1.1	1.0	.9	2.1	1.0	1.0	.9	2.1	1.0
Total Costs (Less CGS)	80.6	101.7	56.6	8.1	120.0	151.6	80.6	13.0	117.0	149.8	78.6	13.0
Total Costs (Less CGS)	8.8	8.9	11.5	9.5	13.5	13.7	17.0	15.7	13.2	13.5	16.6	15.5
Expected Incremental Sales Loss	1.2	1.2	1.9		1.4	1.6	3.1	2.6	-	-	-	-
Year End Expected Total Sales Loss	15.5	15.6	16.2	13.9	22.8	23.2	26.4	23.6	22.2	22.9	25.6	23.0
Expected Savings	17.0	16.9	16.4	18.2	12.5	12.3	10.9	12.2	12.8	12.5	11.2	12.5

* Derivation of these curves is discussed in Chapter 3, Volume I.

FIGURE 5

PRODUCTIVITY COMPARISON^{1/}
MILITARY COMMISSARIES AND COMMERCIAL SUPERMARKETS
 (CONUS)

	<u>WEIGHTED COMMISSARY AVERAGE^{3/}</u>	<u>COMMERCIAL SUPERMARKET</u>
\$ Sales Per Man Year ^{2/}	149,383	81,803 ^{4/}
Sales Per Man Hour ^{2/}	71.82	39.33 ^{4/}
Average Sale Per Transaction	28.05	7.47
Monthly Sales Per Square Foot of Sales Area	65.62	15.12 ^{5/}

Although precise comparisons are not possible due to variations in accounting and allocation of personnel costs, these figures portray approximate productivity between commercial supermarkets and commissary stores.

- NOTE: 1. Commissary statistics are based on Fiscal Year 1974 results and are adjusted to compensate for commercial price differential. Commercial statistics are from Progressive Grocer, April 1974, and Supermarket Industry Speaks, 1974 issue.
2. Man years and man hours include all personnel at store level except warehousemen at Air Force stores.
3. Based on percent of sales by service to total sales:
 Army 35%, Air Force 44%, Navy 18%, Marine Corps 3%.
4. Based on the largest category of commercial supermarkets (above \$2 million sales per year) from Progressive Grocer, April 1974.
5. Industry-wide average. Statistic in Progressive Grocer, April 1974, was not available for the above \$2 million sales category.

CHAPTER 5

POTENTIAL AREAS FOR IMPROVEMENT OF EXISTING SYSTEMS

5-1. GENERAL. In examining areas for possible improvements in the management and operation of commissary stores, the study group has delineated certain areas of present operations that handicap or prevent the commissary store system from attaining maximum efficiency. These potential areas for improvement of existing systems within the various services are described in Volume II, Appendix 5. Also, the American Logistics Association (ALA), an organization whose membership is composed of manufacturers and businessmen who conduct business with commissary stores, was solicited to provide ideas on ways to improve commissary store operations. The ALA report, which is divided into four parts, pricing/promotions, operations, administration, and supplemental data, is attached at Appendix 5-E (Volume II). Those areas of improvement that are applicable to each of the services are discussed below:

a. Management and Administration.

(1) Data Systems. A common accounting and management information system needs to be developed for utilization by all services as a prerequisite to developing hardware and software requirements for an automated data system. The common system would lend itself to useful comparisons between the services and enable the establishment of management controls within the commissary store system.

(2) Automated Data Programs. A system is needed that is capable of handling the high volume of transactions in commissary store operations, which will both highlight requirements for detailed management and reduce administrative costs. Such a system may include electronic Universal Product Code (UPC) scanning at Point of Sales, to permit perpetual inventory and reduce overhead costs.

b. Organization. In an effort to reduce overhead costs, the services need to consider further consolidation, particularly in the areas of administration, procurement, and accounting. Proposed organizations for centralized operations by each service are discussed in Appendix 6 (Volume II). Other functional consolidations could be accomplished if accounting and reporting systems were compatible.

c. Personnel.

(1) Utilization of Other Than Full-time Personnel. Commissary stores employ a high percentage of full-time employees, a practice which is driven by overall base and service manning controls. Due to the assignment of overall employment ceilings, full-time, part-time and intermittent employees count equally against the ceilings, which results in a reluctance on the part of management to hire other than full-time employees. There is a question whether ceiling controls, in addition to existing budgetary controls, promote or hinder the efficient operation of commissary stores. Civilian ceilings can lead to serious and costly inefficiencies. It is a common practice in grocery chains to hire a large proportion of other than full-time employees to meet peak period demand. By eliminating end strength restrictions and/or authorizing the accounting for personnel on a man year basis, other than full-time employees could be utilized to the maximum possible extent, thereby adjusting the total work force as required without incurring additional personnel costs. Paragraph 10-5, page 10-3, shows the amount of savings that can be realized from a proper full-time/part-time mix.

(2) Training and Career Development. An intern program needs to be developed that will insure adequate numbers of personnel qualified in commissary store management. With this career program, recruitment could be made from both the academic environment and from among selected individuals presently employed in the system. The program should incorporate both on-the-job training and attendance at selected government and civilian management training courses. Additionally, functional training courses need to be developed and utilized to a greater extent.

(3) Work Standards. Standards for measuring production efficiency within commissary stores need to be developed and installed. The high volume of product throughput inherent in commissary store operations necessitates that high employee productivity and efficiency be maintained.

d. Operations.

(1) Variable Pricing Structure. The current pricing system is not comparable to that used in the commercial grocery industry. A variable pricing structure, by detailed commodity groups, would allow commissary store management to maximize savings to the patron on essential food items and still provide funds to cover operating costs and other expenses.

(2) Buying Practices. One means for the commissaries to reduce their "every day" prices is through increased participation in the periodic promotions offered by most manufacturers. However, care must be exercised to maintain proper inventory levels.

(3) Vendor Shelf Stocking. Current manpower shortages hamper the shelf stocking effort at most stores which creates out-of-stock conditions. A more liberalized policy on vendor shelf stocking would allow commissary stores to take advantage of such proposals since some vendors may perform this service at no extra cost.

(4) Hours of Operation. Hours of operation should be established to ensure maximum use of personnel to preclude overtime. Store hours could be reduced to a level that provides optimum personnel utilization while concurrently providing adequate customer service.

e. Facilities. Many commissary stores are operated in inadequate facilities that were constructed for other purposes. Although they have been renovated through the years, these facilities are still less than adequate for efficient operations. With construction costs spiraling upward each year, standardization of design could reduce architectural and engineering costs; reduce lead time and construction costs; permit use of modular, pre-engineered construction, where appropriate; and permit standardization of equipment, thus reducing maintenance and the cost of equipment replacement.

f. Miscellaneous. Since commissary stores will reimburse for most direct costs, the triennial price survey should be discontinued. The elimination of the survey and its use as justification for establishment of new stores will allow manpower efforts to be directed toward the performance of regular duties associated with the commissary store operation.

CHAPTER 6

CENTRALIZED SEPARATE-SERVICE COMMISSARY SYSTEMS

6-1 ALTERNATIVE 1. Creation of service-wide commissary management organization to operate separate-service commissary stores.

6-2 ASSUMPTIONS. The assumptions used in developing this concept of centralized service commissary systems were as follows:

a. Operate in an appropriated funded mode with only direct costs reimbursable as defined in section 814 of the annual DOD Appropriations Act.

b. Indirect costs of operations will continue to be supported from appropriated funds.

c. Commissary store civilian personnel will continue to be Civil Service Personnel.

d. Commissary store staffing levels will be commensurate with sales and service levels.

e. Existing stock fund procedures will be modified to accommodate a vertical management structure as required.

f. The subsistence function (troop issue) of the commissary operation will continue to be funded through appropriated funded sources.

g. DSA/DPSC will continue the current support to military commissaries.

h. TRFA/CSRF funds may be invested for the production of additional income as a change to existing policy.

i. TRFA/CSRF funds may be used for construction and renovation of facilities within the U.S.

j. Criteria provisions/restrictions of Section 814 pertaining to establishment and continuation of commissaries will be deleted.

k. A decrease in price differential between the commissary system and commercial stores may result in decreased sales in the commissary system.

l. An effective information program will be implemented to attempt to retain current commissary patronage or recover potential lost patronage that may result from a decrease in savings.

6-3 SUMMARY. The proposals developed for each service to implement this alternative were very similar. Essentially, a commissary management headquarters organization with subordinate regional entities would be established to direct, manage, and control the operation of commissary stores. Current major command responsibilities, obligations, and prerogatives for existing commissary operations would be removed in favor of the vertical structure of alignment and control. Concomitant with such organizational realignments would be programs for consolidation and centralization of functions to accrue the economies of scale proven successful in the Navy commissary system and the civilian retail grocery industry. The detailed write-up of each service proposal is shown in Chapter 6, Volume II.

6-4 SERVICE CONCEPTS

a. Navy.

(1) System Command and Management. Command and management of Navy commissary stores are exercised by the Navy Supplies Systems Command through the Navy Resale System Office. As such, the Navy is currently operating the service-wide commissary management organization defined by this alternative.

(2) Field Organization. Several years ago the Navy commissary system instituted a program of consolidating operational elements into complexes. Consideration would now be given to further consolidations to achieve additional economies. The reduction of the 14 regional complexes down to 9 within the United States appears to be a viable alternative.

(3) Methods of Operation. All Navy stores would continue to operate, under the revised constraints imposed by PBD 282. Any store or region which could not run a break-even operation would be carefully reviewed for continued operation. Where practicable, the 6-day sales week could revert to a 5-day sales week. Efforts would be directed to achieving a full time/other-than-full-time employee mix of 60%/40% respectively. The number of line items and product mix at each activity would be reviewed and changed as necessary to maximize economies of operation. A variable pricing policy would be employed. The supporting ADP capability should be enhanced. The use of military personnel should be discouraged except at isolated locations where qualified civilians are not available. Stores/Regions would reduce warehoused stocks of non-perishable items to not more than 1500 line items. Where professionalized wholesale grocery warehousing and distribution capabilities are available, the economic feasibility of using such facilities would be studied.

(4) Economic Impact and Customer Savings. It is anticipated that sales would decline as initial mark-ons are

increased to generate funds for reimbursement of appropriated fund costs as prescribed by PBD 282. Current savings are estimated to be 22%. The summary of lost sales, required initial mark-ons, and expected customer savings for the transition period is as follows:

	<u>FY 76 and FY 77</u>	<u>FY 77</u>	<u>FY 78</u>
Expected Lost Sales (Incremental)	6.0 - 16.2%	5.9 - 10.2%	0
Required Initial Mark-ons	10.5 - 11.5%	15.3 - 17%	14.0 - 15.4%
Expected Customer Savings	17.4 - 16.4%	12.7 - 10.9%	13.9 - 12.5%

The derivation of these Figures is shown in greater detail in Tables 1 and 2, Pages 6-9 and 6-10.

b. Marine Corps

(1) System Command and Management. A centralized vertical organization with straight line management from the Headquarters Marine Corps (HQMC) is envisioned. The Deputy Chief of Staff for Installations and Logistics would assume direct management and operational control of all Marine Corps commissary stores through a Commissary Store Management Office (CSMO). This office would be responsible for budgeting and accounting, administrative, and operational functions in operating the Commissary Store Program.

(2) Field Organization. Commissary stores on the East Coast and West Coast would be consolidated into two complexes which would permit estimated reductions of 12 - 15% from currently authorized levels. The complex activity would parallel that of the Navy commissary system with the complex office performing administrative, procurement, budgeting and accounting, and operational assistance tasks. The two overseas stores would continue as independent operations.

(3) Method of Operation. Marine Corps installation commanders would be relieved of responsibilities for commissary store operations. The complex officer-in-charge and commissary store officer of independent stores would report directly to the CSMO. Complex officers would maintain all necessary records for branch stores. Revenue from a mark-up on goods sold would be used to pay required expenses and to contribute to the HQMC reserve for construction and capital assets. The mark-up would be variable for each commodity group not to exceed an established maximum percentage. The CSMO would establish the levels of service for all commissary stores including hours of operation, line items authorized, and a never-out list. Day to day operation of branch commissary stores would be managed by a store manager. An operations assistance team would be established at each complex to provide advisory assistance to each store in the complex.

(4) Economic Impact and Customer Savings. As with the other Services, the Marine Corps anticipates that sales will decline as needed mark-up increases. Current savings are estimated to be 22%. The summary of lost sales, required markup, and expected customer savings is as follows:

	<u>FY 76 and FY 77</u>	<u>FY 77</u>	<u>FY 78</u>
Expected Lost Sales (Incremental)	4.8 - 13.9%	5.5 - 9.7%	0
Needed Markup	8.9 - 9.5%	14.3 - 15.7%	14.7 - 15.5%
Expected Customer Savings	18.8 - 18.2%	13.7 - 12.2%	13.3 - 12.5%

The derivation of these figures is shown in greater detail in Tables 1 and 2, Pages 6-9 and 6-10.

c. Army.

(1) System Command and Management. A central management office (CMO) and system of vertical control would be established for operation of the Army commissary system. Under policy guidance and direction from the Deputy Chief of Staff/Logistics, Hq US Army, the CMO would exercise command and management of all commissaries world-wide. Such an organization withdraws responsibility for management and supervision of commissaries from major commands and installations.

(2) Field Organization. Five regional offices would be established under the CMO with responsibility for the operation and control of Army commissaries within their respective geographical areas.

(3) Methods of Operation. Civilian personnel in the commissary stores, regional offices, and the CMO would continue as civil service. The CMO would allocate and control all manpower spaces in the vertical system. Trust revolving funds would be utilized to reimburse appropriated funds for salaries of employees in the commissary stores. A specific condition for future managerial level applicants will be agreement to geographical and organizational reassignments as a condition of employment and career development. A separate resale subsistence division (or separate project code to permit an allocation to the CMO specifically designated for resale) of the Army stock fund would be established with control exercised by the CMO through the field offices for the commissaries within their areas. Field offices would maintain accountability for all commissary assets. Establishment of pricing strategy to generate sufficient revenue to meet prescribed operating costs while affording maximum savings to patrons will be a responsibility of the CMO. The CMO will control the use and investment of commissary cash resources. A world-wide construction program to upgrade existing facilities and construct new facilities where justified will be established and controlled by the CMO. (MCA funds will be used outside the United States for construction). Standard plans and specifications will be utilized

for commissary store facilities. A uniform commissary equipment list will be prescribed by the CMO to meet user requirements at minimum procurement and maintenance costs. Procurement of equipment and supplies will be accomplished primarily at the CMO. Uniform stockage of items world-wide, consistent with customer demand, will be prescribed by the CMO. Computation and consolidation of requirements and preparation of purchase orders will be accomplished primarily by regional offices.

(4) Economic Impact and Customer Savings. Increases in markup are expected to result in reduced sales. Current savings in Army commissaries are estimated to amount to 22.6%. The summary of lost sales, required markups and expected customer savings for the transition period is as follows:

	<u>FY 76 and FY 7T</u>	<u>FY 77</u>	<u>FY 78</u>
Expected Loss Sales (Incremental)	5.8 - 15.5%	3.9 - 7.0%	0
Markup Required	8.1 - 8.8%	11.9 - 13.3%	11.3 - 12.4%
Expected Customer Savings	17.6 - 17.0%	14.1 - 12.7%	14.7 - 13.5%

The derivation of these figures is shown in greater detail in Tables 1 and 2, Page 6-9 and 6-10.

d. Air Force

(1) System Command and Management. The existing system for management of commissary operations would be reoriented to a vertical alignment under an Air Force Commissary Management Office (AFCMO). The AFCMO would function under policy guidance and direction from the Directorate of Maintenance Engineering and Supply, Deputy Chief of Staff/Systems and Logistics, HQ USAF. The AFCMO would be staffed with specialists in the field of commissary operations and sufficient support personnel in funds management, facilities planning and systems development, to plan, operate and control Air Force commissary operations world-wide. Major commands would be relieved of operational commissary responsibilities.

(2) Field Organization. A necessary adjunct to the headquarters organization would be four field offices established to provide technical assistance to base commissaries on a continuing basis to maximize operating efficiency. The field offices would be geographically located to cover the European, Eastern US, Western US and Far East area, with one field office collocated with the AFCMO. Each field office would be responsible for assisting approximately 36 commissaries in their respective areas; it would have no operational functions.

(3) Methods Operation. Coincident to the establishment of the vertical commissary management organization would be a two-phased program leading to the desired end-position of a total organization composed of a headquarters and geographic regions that operate all commissaries, similar to the system presently

utilized by the Navy. Phase I would involve an initial consolidation of the commissary management and administration functions of 16 stores by the establishment of 8 geographical complexes consisting of 2 stores each. Phase II would involve the further consolidation of all commissary stores into regional complexes. The four previously established field offices would be converted into regional headquarters and would be responsible for the centralized performance of all functions except store operations. A data automation capability would be acquired concurrent with implementation of Phase II.

(4) Economic Impact and Customer Savings. A computer simulation has substantiated the expectation that as surcharge rates are increased sales will be lost. Current savings in Air Force CONUS commissaries are estimated to be 22%. The summary of lost sales, required surcharge rates, and expected customer savings is as follows:

	<u>FY 76 and FY 77</u>	<u>FY 77</u>	<u>FY 78</u>
Expected Lost Sales (Incremental)	5.8 - 15.5%	4.5 - 7.5%	0
Required Surcharge Rate	8.1 - 8.8%	12.3 - 13.5%	12.0-13.1%
Expected Customer Savings	17.6 - 17.0%	13.7 - 12.5%	14.0-12.9%

The derivation of these figures is shown in greater detail in Tables 1 and 2, Pages 6-9 and 6-10.

6-5. ADVANTAGES/DISADVANTAGES.

a. The implementation of a centralized management concept would result in the following advantages:

(1) Reduce the layers of command between the Central Management Office and the commissary stores, thereby expediting two-way communication and reporting, permitting prompt resolution of problems at the commissary store level and insuring the uniform implementation of commissary policies and procedures.

(2) Permit reductions in the number of personnel within the commissary system for whom reimbursement must be made. This savings will lower the operating costs which must be recovered from customers; permit greater savings; and reduce sales losses. Savings will also be realized in the number of indirect funded personnel required in support of the system which will reduce appropriated fund costs.

(3) Provide for the concentration of commissary management and technical skills for optimum management effectiveness and improvement of commissary store operations and service. Stores would be able to concentrate exclusively on sales functions.

(4) Provide for total control of the funds and personnel resources required for commissary store operations and permit more precise allocation of these resources on a uniform basis commensurate with workload requirements.

(5) Increase the visibility of all aspects of commissary operations throughout the entire system for the benefit of management in operation and policy decision, and the establishment of priorities for improvement.

(6) Facilitate the grouping of stores within geographic regions with all administrative functions (accounting, bill paying, budgeting, personnel scheduling and payrolls, procurement, stock control, etc.) being accomplished centrally, preclude loss of vendor discounts and achieve a substantial savings in personnel.

(7) Provide a stockage policy which will produce: Uniform stockage criteria, a greater degree of inventory control, item selection based on customer demand, interchange of merchandising information and improved procurement practices through combining the procurement function with determination of requirements and funds authorization.

(8) Relieve commanders and installation staffs of management responsibility for an administrative burden of a technical nature.

(9) Permit more specialized management of commissary personnel, assuring a continuing availability of qualified, motivated personnel, by providing for their training, reassignment executive development and promotional opportunity. This would include establishment of standard position classification and qualifications criteria.

(10) Centralized management will permit the adoption of standardized methods to achieve optimum operating hours and work schedules. Enhanced productivity can be achieved through review and analysis of results obtained and implementation of appropriate management improvements.

(11) Although not directly obtained as a result of centralized management, increased visibility of operations would more readily permit:

(a) Analysis and implementation of more cost effective methods of warehousing and distribution.

(b) Comparison of product costs and selection of methods to achieve the lowest delivered cost for items.

(c) Installing a flexible pricing system designed to maximize patronage of commissaries to achieve additional financial benefits for customers (will require change to existing legislation for Army and Air Force).

b. The implementation of a centralized management concept could result in the following disadvantages (in other than Navy concept):

(1) Remove responsibility for commissary operation from the installation commander while continuing to rely on the installation for certain support. Elimination of this responsibility could result in inadequate emphasis on support of the commissary.

(2) Cause personnel and organizational turbulence during a critical period of changeover to a more self-supporting operation.

(3) Remove responsibility for commissary operations which has previously been viewed by major commands as a function vital to the morale and welfare of their personnel. This disadvantage would be overcome if centralization proved to provide better support and service than at present.

(4) Reorganization will unavoidably shift certain indirect costs (appropriated fund supported) to direct costs (customer borne) at a critical period within the commissary system. To the extent that these costs are not offset by reductions of other direct costs, a significant disadvantage results. Conversely the elimination of the indirect costs provides a quantifiable benefit to appropriated funds.

TABLE 1

ECONOMIC IMPACT AND COST COMPARISON BY
MILITARY SERVICE OF CENTRALIZED
SEPARATE-SERVICE COMMISSARY SYSTEMS

Low Sales Loss - Joint Army/Navy Curve*

ITEM	3/4 FY 1976 & 77			FY 1977			FY 1978		
	A	AF	N	A	AF	N	A	AF	N
Military Service									
Assumed Initial Savings %	22.6	22.0	22.0	22.0	17.6	17.4	18.8	13.6	13.7
Assumed Incremental Sales Loss %	5.5	5.5	5.5	5.5	3.9	3.9	3.9	NO ADDITIONAL	LOSS
Equivalent Supermarket Sales \$M	1223.2	1526.0	660.5	114.3	1457.7	628.7	109.0	1175.7	628.7
Estimated Commissary Sales \$M	1007.8	1257.6	546.0	92.8	1258.6	549.0	94.1	1003.0	541.2
COSTS:									
Cost of Goods Sold \$M	925.9	1155.2	488.8	84.6	1103.5	465.3	80.7	890.0	465.3
Cost of Goods Sold %Sales	91.9	91.9	89.5	91.2	87.7	84.8	85.6	88.7	86.0
Personnel \$M	46.0	54.5	27.9	3.8	109.7	56.2	9.3	79.7	49.5
Personnel %Sales	4.6	4.3	5.1	4.1	8.7	10.2	9.9	7.9	9.1
Operations \$M	26.6	36.3	19.2	3.5	34.4	17.6	3.4	23.3	16.5
Operations %Sales	2.6	2.9	3.5	3.8	2.7	3.2	3.6	2.3	3.8
Capital Outlay \$M	9.3	11.6	10.0	.9	11.1	10.0	.8	10.0	10.0
Capital Outlay %Sales	.9	.9	1.8	1.0	.9	1.8	.9	1.0	.8
Total Costs (Less CGS) \$M	81.9	102.4	57.1	8.2	155.1	83.8	13.5	113.0	76.0
Total Costs (Less CGS) %Sales	8.1	8.1	10.5	8.9	12.3	15.3	14.3	11.3	14.0
Expected Incremental Sales Loss %	.3	.3	.5	.5	.6	2.2	1.6	NO ADDITIONAL	LOSS
Expected Savings %	17.6	17.6	17.4	18.8	13.7	12.7	13.7	14.7	13.9
Expected Total Sales %	5.8	5.8	6.0	4.8	10.3	11.9	10.3	8.8	9.9
Loss									

* Derivation of these curves was discussed in Chapter 3, Vol I.

TABLE 2

ECONOMIC IMPACT AND COST COMPARISON BY
MILITARY SERVICE ON A CENTRALIZED
SEPARATE-SERVICE COMMISSARY SYSTEM

High Sales Loss - DOD Curve*

ITEM	3/4 FY 1976 & 77				FY 1977				FY 1978			
	A	AF	N	MC	A	AF	N	MC	A	AF	N	MC
Military Service												
Assumed Initial Savings %	22.6	22.0	22.0	22.0	17.0	17.0	16.4	18.2	12.7	12.5	10.9	12.2
Assumed Incremental Sales Loss %	14.3	14.3	14.3	14.3	7.1	7.1	7.1	7.1	7.1	7.1	7.1	7.1
Equivalent Supermarket Sales \$M	1099.6	1371.3	590.6	103.8	1004.2	1267.1	532.0	94.3	1004.2	1267.1	532.0	94.3
Estimated Commissary Sales \$M	912.8	1138.6	493.6	85.0	876.6	1109.2	474.3	82.8	868.3	1104.2	465.6	82.5
COSTS:												
Cost of Goods Sold	832.4	1038.1	437.1	76.8	760.2	959.2	393.7	69.8	760.2	959.2	393.7	69.8
Cost of Goods Sold	91.2	91.2	88.6	90.4	86.7	86.5	83.0	84.3	87.6	86.9	84.6	84.6
Personnel	46.0	54.5	27.9	3.8	86.4	109.7	56.2	9.3	79.7	106.6	49.5	9.3
Personnel	5.0	4.8	5.6	4.5	9.9	8.9	11.8	11.2	9.2	9.7	10.6	11.3
Operations	25.4	35.6	18.7	3.4	21.2	30.7	14.4	2.9	19.7	28.8	12.4	2.7
Operations	2.8	3.1	3.8	4.0	2.4	2.8	3.3	3.5	2.3	2.6	2.7	3.3
Capital Outlay	9.0	10.4	10.0	.9	8.8	9.6	10.0	.8	8.7	9.6	10.0	.8
Capital Outlay	1.0	.9	2.0	1.1	1.0	.9	2.1	1.0	1.0	.9	2.1	1.0
Total Costs (Less CGS)	80.4	100.5	56.6	8.1	116.4	150.0	80.6	13.0	108.1	145.0	77.9	12.8
Total Costs (Less CGS)	8.8	8.8	11.5	9.5	13.3	13.5	17.0	15.7	12.4	13.1	15.4	15.5
Expected Incremental												
Sales Loss	1.2	1.2	1.9			.6	3.8	2.6	NO	ADDITIONAL	LOSS	
Expected Savings	17.0	17.0	16.4	18.2	12.7	12.5	10.9	12.2	13.5	12.9	12.5	12.5
Year End Expected Total												
Sales Loss	15.5	15.5	16.2	13.9	22.5	23.0	26.4	23.6	20.9	22.2	22.9	23.0

* Derivation of these curves was discussed in Chapter 3, Vol I.

CHAPTER 7

ALTERNATIVE 2

CONSOLIDATION OF COMMISSARY SYSTEMS WITH EXISTING EXCHANGE SYSTEMS

7-1. OBJECTIVE. The objective of this alternative is to merge the commissary store system of each service with its respective exchange system. The Navy and Marine Corps Commissary Systems would merge with the respective Navy Exchange and Marine Exchange System. However, the Army and Air Force Commissary Systems (excluding Troop Issue) would be merged with one exchange system, the Army and Air Force Exchange System (AAFES). The merger of commissary stores with exchange systems would enable both systems to derive economies of operations from the existing centralized operations of the exchange systems. The detailed writeups of each service proposal are shown in Chapter 7, Volume II.

7-2. ASSUMPTIONS. The assumptions used in developing this concept are as follows:

- a. Army and Air Force commissary stores will merge with AAFES.
- b. No commissary will be operated on a concession basis.
- c. The system will operate in non-appropriated fund mode with personnel temporarily remaining as appropriated funded on a reimburseable basis.
- d. The following items will be turned over to the appropriate exchange service on a non-reimburseable basis:
 - (1) Equipment and supplies.
 - (2) Current financial assets generated in compliance with Section 814 of the Department of Defense Appropriations Act.
 - (3) Stock funded inventory on hand and on order.
- e. The common support functions currently rendered to the exchange systems at installation level will continue to be provided, except for utilities overseas.
- f. Appropriated funds will pay severance cost of Civil Service employees.
- g. All procurement, including items procured through DPSC, will be directed through the applicable exchange service.
- h. Civil Service personnel, currently engaged in installation level commissary store operations, will be provided an opportunity to secure non-appropriated fund employment with the commissary system.
- i. Commissaries will operate on a non-profit basis with no contribution to welfare and recreation funds.

j. Troop issue function will not be absorbed by the exchange service systems.

k. Locations at which commissaries will be operated will be as determined by the Secretary of the appropriate military department.

l. Criteria currently contained in Section 814 Annual Appropriations Act, concerning establishment and discontinuances of commissary stores will be deleted.

7-3. FUNDING

a. Facilities. Commissary store and warehousing facilities currently being utilized for commissary operation, although generally in need of improvement, would continue to be operated for these purposes.

b. Working Capital. The exchange services would require additional capital at the time that exchanges and commissaries are merged. This would be accomplished by turning over to the exchange services the following items on a non-reimbursable basis.

(1) Equipment and supplies provided from Commissary Store Reserve Funds.

(2) Current financial assets generated in compliance with Section 814 of the Department of Defense Annual Appropriations Act.

(3) The stock funded inventory on hand and on order.

(4) Change funds currently in use in commissary stores.

c. Personnel Costs. Personnel costs would become the responsibility of non-appropriated funds after the merger of commissary stores with exchanges. However, personnel currently employed by commissary stores are Civil Service employees paid from Congressional appropriations. Therefore, at the time of merger, reduction in force action would be required. The severance costs resulting from the reduction in force action would be the responsibility of appropriated funds.

7-4. PERSONNEL

a. General. The most critical problem in the merger of commissaries with exchanges is in the area of personnel. Civilian personnel currently employed in commissary stores are Civil Service employees. Should commissary stores merge with exchanges, the personnel would become non-appropriated fund employees. Consequently, the possible loss of Civil Service benefits, such as retirement, seniority, sick leave, etc., could have a detrimental effect on morale, and it is likely that many of the personnel would

attempt to obtain other Civil Service positions rather than convert to non-appropriated fund employment. However, in view of the unique specialized skill requirements of the commissary store supervisory and skilled positions, the probability of an excessive loss of supervisory, management and skilled clerical workers is unlikely.

b. Transition Period. In accordance with Program/Budget Decision 282, 50% of the personnel costs of commissary stores are to be reimbursed for the period 1 October 1975 to 30 September 1976. After 30 September 1976, commissary stores will be required to absorb 100% of the personnel costs.

(1) Classification. Personnel currently employed in commissary stores would remain Civil Service personnel until 30 September 1976.

(2) New Employees. Effective 1 October 1975, all non-management personnel hired by commissary stores would be hired as appropriated fund temporary employees.

(3) Position Descriptions. During the transition period, position descriptions and job grades must be developed for all positions in accordance with NAF procedures.

(4) Wage Surveys. Wage surveys would be conducted in accordance with NAF procedures, in order that they may be implemented on 1 October 1976.

(5) Reduction in Force. Reduction in force notices must be given to commissary employees in accordance with time frames required by Civil Service procedures.

(6) Reemployment. Offers of employment, outlining positions and salary offered, would be forwarded to commissary personnel. The offers of employment would also outline benefits of NAF employment such as qualified personnel would be able to retire (either regular or involuntary) from Civil Service and build further retirement benefits through NAF retirement programs and Social Security. The offer of employment would allow sufficient time to enable personnel to properly evaluate the offer and determine the appropriate action.

c. Training. Training programs and schedules would be established in order that personnel would be properly trained in the required non-appropriated fund procedures.

d. Appropriated Fund Costs. The payment of severance costs, including accrued vacation would be the responsibility of appropriated funds. Payment of accrued leave would approximate \$20 million and potential severance pay costs would be approximately \$54 million dollars. (See Appendix 10-A, Volume II).

e. Personnel Policies. Effective with the transfer of employees from Civil Service to non-appropriated fund employment, the employees would become subject to the personnel policies of the applicable exchange system.

7-5. OPERATIONAL and COMMAND METHOD

a. Method of Operation. If commissary stores are merged with exchanges, they would be operated as departments of the exchanges, permitting adjustment of store hours to meet customer requirements. Integration of commissary stores with exchanges would permit the utilization of common support services, avoid costs of duplication of functions and enable the most effective utilization of available expertise.

b. Headquarters Organization. The headquarters of each exchange system would assume command control of the integrated commissaries and exchanges. This is another major problem due to the difference in organizational structure of the respective services, exchange and commissary stores. Effective integration of these resale activities would require transfer of command responsibilities from installation to the headquarters of each exchange system as follows:

(1) Army and Air Force: Command responsibilities for commissary stores would be transferred from the installation commander to Commander, Army and Air Force Exchange Service.

(2) Navy: Command responsibilities for exchanges would be transferred from installation level to Commanding Officer, Navy Resale System Office.

(3) Marine Corps: Command responsibilities for commissary stores and exchanges would be transferred to the Head of the Marine Corps Exchange Service. (Appendix 7C presumed that the present commissary system would be merged with the exchange service, but that command responsibilities would remain at installation level.)

c. Field Organization: All functions would be aligned with and integrated into the existing types of exchange organizational alignments and would be at the organizational level at which exchange functions are accomplished.

d. Staffing. The staffing of the integrated system would take cognizance of the differences in the operation of grocery stores and department stores and will provide for the necessary expertise at each management level to insure the required specialized attention and effective management control.

7-6. DISTRIBUTION SYSTEM. The merger of commissary stores and exchanges would place an increased burden on warehousing and distribution facilities and equipment. The most economical method of distribution, such as central distribution, commercial distribution facilities, direct delivery and vendor shelf stocking would be utilized. As improved warehousing and distribution facilities become available, by construction of new facilities, renovation of existing facilities, or the availability of additional government buildings, distribution procedures would become more cost effective.

7-7. DATA SYSTEMS.

a. Army and Air Force Exchange Service. AAFES merchandise control programs, including accounts payable, are fully automated. This includes a data link from each store to the main computer and provides for utilization of modern techniques for inventory management. Some of the merchandise inventory

management programs can be used for control of commissary items without extensive modification to existing programs. Additionally, AAFES has mechanized payroll, personnel management information systems, and check cashing controls which could be adapted to commissary store procedures with minimal modification.

b. Navy Resale System. Navy commissary stores utilize first generation, solid state, general purpose, stored program, digital computers to accomplish procurement and accounting functions. These computers are located at each regional office and at most independent stores. Navy Exchange Service Centers in San Diego and Jacksonville have more sophisticated computer capability and have instituted merchandise control systems. Fully automated merchandise control systems with a data link to the Navy Resale System Office for Navy Exchanges and Commissary Stores are being developed and will be tested by the commissary region at Norfolk prior to system wide implementation.

7-8. MERCHANDISING AND PROCUREMENT. Changing of the product mix by the addition of impulse type houseware items in all commissaries, and soft drinks, candy, and tobacco products in Navy commissary stores, and tobacco products in Marine Corps commissary stores would provide better service to customers. Variable markups would be used to maintain item prices under the commercial sector to the fullest extent possible. The consolidation and centralization of computerized requirements determination would produce savings in the cost of procured merchandise. However, as explained in Volume II Appendix 7-D, the absorption of the DPSC resale procurement functions by the integrated commissary and exchange system would result in the fragmentation of the DPSC IMM subsistence responsibilities, make the troop issue mission uneconomical, reduce the mobilization base and result in a significant reduction in force. Therefore, the possibility of DPSC continuing their current support functions to commissary stores must be investigated.

7-9. ACCOUNTING AND RELATED FUNCTIONS. The integration of commissaries with exchanges would permit the adaptation of cash handling, accounting and personnel procedures currently in effect in the exchange systems. The consolidation would result in the reduction of employees currently employed in the separate commissary and exchange offices. Additionally, although the Study Group did not fully assess the impact in this area, it is assumed that some Civil Service positions would be reduced at the various bill paying, accounting and auditing offices.

7-10. ECONOMIC IMPACT. The proposal in PBD #282 that commissary stores absorb personnel costs and the cost of utilities overseas would result in reduced customer savings and, as a consequence, reduced sales in commissary stores. The merger of commissary stores with exchanges would permit the avoidance of the costs of duplication by utilizing common support functions, such as accounting, procurement, personnel management, administration and distribution, thereby lessening the

economic impact of PBD #282. Considering that FY 1976 and FY 1977 require reimbursement of 50 percent of the direct costs, FY 1977 will be the transition year in which the full impact of PBD #282 will be felt. Tables 1 and 2 indicate that in FY 1978 the expected savings percent will range from 11.9 to 14.2 percent and that the year-end expected sales loss will be from 9.6 percent to 24.0 percent. The difficulty in predicting the reaction of customers is the cause of the wide fluctuations in Tables 1 and 2. The possibility exists that more meaningful savings can be provided to customers as more efficient procedures are developed and facilities are improved.

7-11. ADVANTAGES AND DISADVANTAGES. The merger of commissary stores with exchanges presents several advantages and disadvantages such as those listed below:

a. Advantages.

- (1) Meaningful customer savings through the expansion of product mix and use of variable markup.
- (2) Greater flexibility in adjusting store hours to customer requirements.
- (3) Improved ability to accommodate changing and/or fluctuating sales trends.
- (4) Greater flexibility in management of personnel such as more rapid hiring, promotion, and reassignment of employees, adjustment of schedules, greater use of part-time employees.
- (5) Consolidation of administration, accounting, data services, procurement and payroll functions.
- (6) Easy adoption of current exchange procedures.
- (7) Centralized overall management of exchanges and commissaries.
- (8) Reduction of current overall direct wage costs in commissary stores.
- (9) Increased cash flow providing more monies for investment.
- (10) System efficiencies and broader base for financing overhead costs provided by merger of exchange and commissary stores facility, personnel, monetary, and inventory assets.
- (11) Savings of \$258 million annually in appropriated funds. Reduction of current indirect support of commissary stores in area of

procurement, bill paying, personnel administration accounting and audit functions now being performed by installations and DPSC will result in additional appropriated fund savings.

b. Disadvantages.

(1) The time frame of 1 October 1976 (for implementation of PBD #282) is not realistic for this alternative.

(2) Possible discontinuance of DPSC services.

(3) Potential excessive loss of management personnel due to conversion to non-appropriated funds.

(4) Adverse effect on employee performance at a critical period by changing from Civil Service to NAF.

(5) Increased cost of personnel fringe benefits.

(6) Absorption of cost for items of indirect support such as procurement, bill paying, payroll and audit due to the consolidation.

(7) Current inadequate exchange and commissary facilities.

(8) Initial costs of reorganization.

7-12. LEGISLATIVE CHANGES. Legislative changes required for implementation of the merger of commissary stores with exchanges are contained in Chapter 11.

TABLE 1

ECONOMIC IMPACT AND COST COMPARISON BY MILITARY SERVICE OF SELECTED ALTERNATIVES
ALTERNATIVE #2 - CONSOLIDATION OF COMMISSARY SYSTEMS WITH EXISTING EXCHANGE SYSTEMS
LOW SALES LOSS - JOINT ARMY/NAVY

ITEM	3/4 FY 1976 & 77				FY 1977				FY 1978			
	AAFES	SEV Gp Est*	N	MC	AAFES	SEV Gp Est	N	MC	AAFES	SEV Gp Est	N	MC
Military Service												
Assumed Initial Savings	%											
Assumed Incremental Sales Loss	%											
Equivalent Supermarket Sales	\$M	2672.7	2672.7	5.5	2598.4	2555.8	646.9	108.7	2598.4	2555.8	650.3	108.7
Estimated Commissary Sales	\$M	2272.5	2288.3	546.0	2266.8	2257.1	568.0	93.4	2253.4	2250.9	560.0	93.3
Costs:												
Cost of Goods Sold	\$M	2020.0	2004.0	488.8	1946.9	1916.3	472.7	81.5	1946.9	1916.3	473.3	86.6
Cost of Goods Sold	\$M	88.9	87.6	89.5	86.3	84.9	83.2	87.3	86.4	85.1	84.5	87.5
Personnel	\$M	165.4	179.0	27.9	224.9	239.6	59.3	8.4	223.4	236.3	50.4	8.4
Operations	\$M	7.3	7.8	5.1	10.0	10.6	10.4	9.0	9.9	10.5	9.0	9.0
Operations	\$M	67.8	84.1	19.2	64.6	80.1	25.1	2.5	62.8	78.0	25.1	2.5
Capital Outlay	\$M	3.0	3.7	3.5	2.9	3.5	4.4	2.7	2.8	3.5	4.5	2.7
Capital Outlay	\$M	19.3	21.3	10.0	20.3	21.1	10.9	1.0	20.3	20.3	10.9	.9
Total Costs (less CGS)	\$M	.8	.9	1.8	.9	.9	1.9	1.1	.9	.9	1.9	1.0
Total Costs (less CGS)	\$M	252.5	284.3	57.1	309.8	340.8	95.3	11.9	306.5	334.6	86.4	11.8
Expected Incremental Sales Loss	\$M	11.1	12.4	10.5	13.7	15.1	16.8	12.7	13.6	14.9	15.4	12.6
Year End Expected Total Sales Loss	%	3.0	3.8	.5	.3	1.0	.8	.7	NO ADDITIONAL SALES LOSS			
Expected Savings	%	8.5	9.3	6.0	11.1	13.7	12.2	9.7	10.6	13.2	9.9	9.6
	%	15.0	14.4	17.4	13.2	11.7	12.7	14.1	13.3	11.9	13.9	14.2

*For explanation of Study Group Estimate, refer to para 7-A.3f, page 7A-3, Volume II.

ECONOMIC IMPACT AND COST COMPARISON BY MILITARY SERVICE OF SELECTED ALTERNATIVES
ALTERNATIVE #2 - CONSOLIDATION OF COMMISSARY SYSTEMS WITH EXISTING EXCHANGE SYSTEMS
HIGH SALES LOSS - DOD CURVE

7-9

*For explanation of Study Group Estimate, refer to para 7-A.3f, page 7A-3, Volume II.

CHAPTER 8

JOINT SERVICE COMMISSARY STORE AGENCY

8-1. ALTERNATIVE. To merge the service commissary stores into a joint service administered system. (A detailed discussion of this alternative is contained in Appendix 8-A, Volume II.)

8-2. ASSUMPTIONS. This concept considers the following assumptions:

a. Operate in an appropriated funded mode with only direct costs reimbursable as defined in the currently proposed section 814 of the annual DOD Appropriations Act.

b. Continue support of indirect costs of operations from appropriated funds.

c. Exercise direct command and control of the commissary store system with the Joint Service Commissary Store Agency (JSCSA).

d. Activate the JSCSA with personnel from each service with background in management of commissary stores.

e. Draw manpower authorizations for the JSCSA by transfer of function from the individual services.

f. Exercise complete control over JSCSA manpower authorizations. Vest authority to distribute and redistribute spaces to each commissary operation in JSCSA.

g. Continue civilian employees in the competitive career Civil Service program on a reimbursable basis, in accordance with the proposed section 814, of the annual DOD Appropriations Act.

h. Staff commissary stores commensurate with sales and established levels of service.

i. Consolidate applicable portions of individual service stock funds into a Joint Service Commissary Stock Fund.

j. Transfer to the commissary agency each service's Trust Revolving Fund Account (TRFA)/Funds and Commissary Store Reserve Funds (CSRF), upon implementation of the system.

k. Invest TRFA/CSRF for the production of additional income.

l. Continue to provide Defense Supply Agency (DSA) and Defense Personnel Support Center (DPSC) support to commissary stores.

m. Separate the subsistence function (troop issue) from the commissary operations.

n. Delete or modify the criteria/provisions of section 814 of the annual DOD Appropriations Act pertaining to establishment and continuation of commissary stores.

o. Develop a standard management and automated data processing system prior to implementation of the Joint Service Commissary Store system.

8-3. HEADQUARTERS AND FIELD ORGANIZATION.

a. This alternative provides for the establishment of a Joint Service Commissary Store Agency (JSCSA) which shall have command, control, and direction over the worldwide system of commissary stores. In addition to the JSCSA, the organization shall consist of seven regional offices and 34 field offices having cognizance over 265 stores in CONUS; three regional offices and 16 field offices controlling 83 stores in Europe; and one regional office and eight field offices controlling the activities of 36 stores in the Pacific. Figures 4 and 5 of Appendix 8A, Volume II (pp 8A-21 and 22), provide details concerning the geographical boundaries of the proposed regions and area field offices including the specific stores to be serviced. Figures 1 through 3 of the same Appendix (pp 8A-15 to 20) provide details concerning the proposed organizational structures and manning requirements.

b. JSCSA would be established as a separate command under the jurisdiction of the Chiefs of Staff of the Army and Air Force, the Chief of Naval Operations, and the Commandant of the Marine Corps. A board of directors, representing each of the military services would be responsible for directing the operations of JSCSA. JSCSA would provide policy guidance and direct the plans and programs of the worldwide commissary store system. In addition, JSCSA would review the financial status of the system and assure that it is responsive to the needs of authorized patrons.

c. The regional offices would provide procurement, accounting, automatic data processing, and administrative support to the commissary stores within each region.

d. The field offices within each region would be responsible for providing day to day technical management, advice, and assistance to the stores under their jurisdiction, and for maintaining liaison with commands represented.

8-4. ESTABLISHMENT/DISESTABLISHMENT OF STORES.

a. This alternative provides that the Secretary of Defense will authorize the establishment of commissary stores. The board of directors may authorize the disestablishment of stores.

b. The possibility of reducing the number of commissary stores, where such action will produce significant economy without seriously impairing customer service, will be reviewed by the JSCSA.

8-5. FUNDING.

a. Facilities. Store and warehouse facilities currently in use are in need of improvements. Current facility and equipment deficiencies of the combined service commissary systems are estimated to total \$408.6 million. The additional funding burden imposed by PBD #282 precludes the generation of sufficient additional revenue from surcharge to finance the extent of new construction and renovation which is urgently needed to upgrade facilities appropriately. Consequently, it is recommended that the Department of Defense consider requesting one time appropriations for this purpose.

b. Working Capital. The following would be transferred to the Joint Service Commissary Agency on a non-reimbursable basis:

(1) Equipment and supplies provided from Commissary Store Reserve/Surcharge Funds.

(2) Financial assets generated in compliance with Section 814 of the Department of Defense Annual Appropriations Act.

(3) Stock funded inventory on hand and on order. Following is a breakdown of sales and inventory levels for all services for fiscal year 1974:

	Sales CONUS	Overseas Sales	(CONUS) Monthly Stock Level Limitations	(Overseas) Monthly Stock Level & In Transit
Air Force	930.7M	134.3M	77.6M	33.6M
Army	719.1M	191.8M	59.9M	48.0M
Navy	405.8M	58.6M	33.8M	14.7M
Marine Corps	75.7M	1.3M	6.3M	.3M
	\$2,131.3M	\$386.0M	\$177.6M	\$96.6M

c. Personnel Costs. Personnel in the commissary stores, field offices, regional headquarters, and central headquarters will be Civil Service employees paid from Congressional appropriations. In addition military personnel shall be utilized in certain key management positions at headquarters and regional level and at isolated overseas locations too small to justify the assignment of civilian personnel. Appropriate reimbursement for the cost of Civil Service and military personnel shall be made from commissary store surcharge funds in accordance with the provisions of PBD #282.

8-6. PERSONNEL.

a. Retention of Civil Service employees will ensure continuity

of operations and avoid costly expenses which would be required to sever, rehire, and retrain employees in a non-appropriated funded mode.

b. Under this alternative the central management agency (JSCSA) will control personnel resources. Accordingly, it is envisioned that improved personnel resource utilization will result. Some of the benefits to be gained are improved utilization of part-time and intermittent employees, standardization of work processes, use of performance standards, and the establishment of a series of basic training courses which can be administered at the work location utilizing programmed learning technology.

8-7. OPERATIONAL MODE.

a. Headquarters Organization. Effective integration of commissary stores of the respective services will require transfer of command responsibilities to the Commander, JSCSA.

b. Field Organization. Realignment shall generally conform to the organization as indicated in Figures 4 and 5, Appendix 8A, Volume II (pp 8A-21 - 8A-33).

c. Staffing. Figures 2, 3 (pp 8A-16 - 8A-20), 6 and 7 (pp 8A-34 - 8A-35), Appendix 8A, Volume II, detail staffing requirements.

8-8. DISTRIBUTION SYSTEM. This alternative offers the opportunity to provide centralized local management of stores in the same general geographic area which are presently being managed by different services. This in turn will afford economies in the areas of warehousing and distribution. Options such as the consolidation of warehousing and distribution capabilities, availability of commercial distribution facilities, use of central meat cutting or produce processing plants, and utilization of materials handling and transportation equipment will be explored. Overseas distribution systems will be revised to incorporate joint service use of the DICOMSS system.

8-9. ASSUMPTION OF CONTROL. This could be accomplished in 3 to 5 years on a phased basis as follows:

a. Phase I - Form a skeletal commissary store headquarters organization to develop plans for the organization and a plan of action with time frames for accomplishment.

b. Phase II - Develop a staffing plan, detailed operating, accounting and ADP procedures.

c. Phase III - Establish field organizations on a phased basis.

8-10. DATA SYSTEMS. The development of uniform accounting, reporting, and automated systems within the JSCSA is a necessary prerequisite to the merger into a joint service organization. ADP applications must include programs for inventory/financial control, stock replenishment, purchasing, cash and charge sales, and future use of the Universal Product Code. Preliminary studies indicate that ADP hardware capable of supporting system-wide needs will cost approximately \$15.5 million. Approximately 252 man-months will be required over an 18-month period for development of the necessary program applications. Further discussion of ADP support requirements is contained in Annex A, Appendix 8-A (p 8A-39), Volume II.

8-11. MERCHANDISING. This alternative will utilize variable markups in order to maintain item prices under the commercial sector to the fullest extent possible. It also provides for the standardization of product categories and product mix where practicable. Maximum opportunity shall be afforded to purchase carload or special lots resulting in a lower cost of goods. Also, uniform controls over buying will ensure maximum utilization of vendor promotional sales, offers such as guaranteed sales, floor stock protection, special label merchandise, voluntary price reductions, and bonuses.

8-12. PROCUREMENT.

a. Presently employed procurement practices, utilizing the services and facilities of the Defense Personnel Support Center, will continue. (See Appendix 7-D, Volume II (p 7D-1).)

b. Regional offices shall determine requirements, select items, prepare purchase documents, and account for receipts.

c. JSCSA will perform the procurement functions for equipment and facilities replacement and develop centralized procurement policies for those items that will result in greater savings.

8-13. ACCOUNTING. Uniform procedures will be developed for cash handling, bill paying, payroll, auditing, and personnel administration.

8-14. SUPPORT MISSION. Whereas, the assumptions provide that the troop issue support function shall be divorced from the resale function, it is recognized that the storage capabilities at certain locations may be sufficient to support both resale and troop issue requirements. In such instances such additional requirements could be supported, provided appropriated fund reimbursement could be made to the servicing commissary store.

8-15. ECONOMIC IMPACT.

a. PBD 282 requires that commissary stores absorb personnel costs and the cost of utilities overseas. This in turn will reduce commissary store sales. FY 1976 and FY 1977 will require reimbursement of 50% of

the direct costs and FY 1977 will be the transition year in which the full impact will be felt. Table 1, Appendix 8A, Volume II (p 8A-37) indicates that in FY 1978, the expected savings percent will range from 13.4 to 14.3 percent and that the year-end expected sales loss will range from 9.3 to 21.2 percent. The difficulty in predicting customer reaction accounts for the wide fluctuations in expected sales loss.

b. Table 1 does not reflect any savings which may be realized through the reorganization, improved utilization of personnel, economies of scale, improvement of facilities, or the acquisition of ADP capability; however, it is assumed that these will contribute favorably to the production of more meaningful savings.

8-16. COST ANALYSIS. Figure 8, Appendix 8A, Volume II (p 8A-36) provides a cost analysis of the JSCSA which includes savings realizable from the elimination of current headquarters and installation level support. This analysis indicates that cost reductions approximating \$13 million can be realized by adopting this alternative.

8-17. ADVANTAGES AND DISADVANTAGES.

a. Advantages. Implementation of this alternative will result in the following advantages:

- (1) A single professional organization for the management of commissary activities and development of uniform operating policies worldwide.
- (2) Uniform policies and operations for equitable commissary savings and service for all military personnel and their dependents.
- (3) Maximum visibility of the overall operation of commissary stores.
- (4) More effective utilization of funds, facilities, equipment, and personnel through improved management and greater standardization.
- (5) The potential will be created for significant economies in such areas as procurement, storage, and distribution.
- (6) The potential for improved commissary personnel management in the areas of staffing, position standards, training and development, and career progression will be developed.
- (7) Continued use of central Civilian Personnel Office, Defense Personnel Support Center, and finance paying office appropriated funded support.

(8) A more viable and efficient organization through merger of headquarters level assets.

(9) Avoidance of legislative, personnel, and operational changes which would be required in a non-appropriated funded mode.

b. Disadvantages. The implementation of this alternative will result in the following disadvantages:

(1) Will be a major undertaking, involving a substantial expenditure of funds for the relocation of personnel in the establishment of new organizations.

(2) Might be viewed by some as the creation of a large and unwieldy business entity.

(3) Will result in significant temporary personnel turbulence due to organizational realignments.

(4) Possible reduction of local command support of commissary stores.

(5) Cannot be accomplished within the time frame of PBD 282.

8-18. LEGAL ASPECTS. Chapter 11 discusses legal and legislative requirements in detail. Basically, no new legislation is required to create a Joint Service Commissary System. However, certain legislative changes are necessary to allow such a system to operate effectively.

CHAPTER 9

CONTRACT OPERATION OF COMMISSARIES

9-1. GENERAL.

a. A possible method of operating military commissary stores is to contract for their operations either on a concession basis or under a service contract for management and labor. The purpose of this study is to determine the feasibility of contract operation of commissaries.

b. Discussions were conducted with officials of several leading supermarket chains. These contacts were initiated to obtain the general views of industry as to how military commissary stores could be more efficiently operated and to explore the alternative of industry operating military commissary stores.

c. Care was exercised to insure that officials contacted appreciated the fact that this alternative was one of a number of alternatives being examined and that no obligation or commitment to any future action existed on the part of the government.

d. For comparability with other analyses, contract operation has been examined on the basis that the contractor would generally be responsible for all phases of commissary operations (such as provision of management and labor, requirements determination, procurement, distribution, storage, display, etc.). It is recognized that a more limited contractual method, for example, contractor provided management and/or labor only, could be developed. However, restricting the study to one or more specific limited contractual methods would have precluded the analysis of total operation which was determined to be warranted.

9-2. RESULTS OF INDUSTRY CONTACTS. Following is a summary of major considerations obtained from the study group discussions and field contacts with members of industry.

a. Commercial interest was generally limited to the geographical marketing area of the firm concerned. Although one firm did indicate some interest in a CONUS-wide management service arrangement, it may be assumed that if contract operation were selected, contracts with several firms would be required within the United States. Contract administration costs covering several different contracts would be higher than if a single firm were involved. An equally important consideration is that it would be difficult to maintain equivalent standards of service and comparable prices for commissary patrons.

b. With one exception, there was no interest expressed in contracting for overseas operation. The exception involved contracting for

management and labor only. It would, therefore, be necessary to retain much or all of the existing overhead structure (e.g., distribution system, policy determination, financial controls, etc.) for the overseas commissary system under this method. Spreading these overhead structure costs across the limited base entailed by overseas operations, could result in prohibitive price increases to patrons.

c. All discussions indicated that customer savings under commercial contract operation would be significantly less than would be obtained under any other alternative examined by the study group. In one instance, there was an indication that savings in the range of five to six percent might be obtainable. Separate study group projections indicate savings of this limited magnitude would cause major (30 to 50%) losses of sales. These losses would represent a total loss of the value of the benefit for those who would no longer shop in the commissary and a major reduction in the value of the benefit for those who continue to shop.

d. A major difficulty in contracting for the total operation of a business of the size of commissaries would involve duration of the contract. Contractor operation would require major capital investments which could only be amortized over a period of many years unless prices charged customers were raised to prohibitive levels. Similarly, frequent changes of management, which could occur in a management and labor services type contract, would disrupt the effectiveness of the system and result in high prices being charged to customers. Discussions with industry representatives confirmed that short term contracts (e.g., one year renewable for four years) would be inadvisable for both the government and industry.

9-3. COMPARISON OF RELATIVE PRODUCTIVITY AND PERSONNEL COSTS.

a. Productivity comparisons between military commissaries and commercial supermarkets are contained on figure 3, Chapter 4, Volume 1, for dollar sales per man year, dollar sales per man hour, average sale per transaction, and monthly sales per square foot of sales area. They show that military commissaries generally have higher productivity than their commercial counterparts.

b. The July 1974 Fortune magazine reported that a retail food enterprise having sales of about \$3.2 billion, which is comparable to commissary store sales of \$2.5 billion, employs approximately 42,600 personnel. This staffing level within the commercial sector is 1.6 times greater than the approximately 27,000 personnel who operated the commissary system in fiscal year 1974. Using data in the same magazine, a commercial supermarket chain with sales equivalent to those of the commissary system would be operating approximately 1470 stores as opposed to the military's 400 plus stores.

c. The relatively higher productivity of commissaries is partly

attributable to two major factors:

(1) Customer service is maintained within commissaries at lower levels than in commercial supermarkets. For example, queuing, i.e., waiting for parking space, to enter the store, and in checkout lines is prevalent in commissaries and is generally accepted by patrons in order to obtain the savings provided.

(2) Commissaries currently have significantly higher average sales volumes than supermarkets. This factor supports the achievement of relatively higher productivity in commissaries. Anticipated sales losses will impact on this situation.

d. Personnel costs, as a percent of sales, provide another basis for comparison. Personnel costs within commissaries average 7.66 percent of sales when adjusted for comparable supermarket prices. This compares with industry's store level personnel costs which average 8.55 percent of sales (for supermarket chains with annual sales above \$500 million). In this comparison, the commissary figure includes fringe benefits plus office and warehouse personnel costs which are excluded from the commercial costs used.

e. Commercial chain personnel costs represent more than 50 percent of their total operating costs. Because of this high percentage relationship to total operating costs, comparison of potential personnel costs for commercial contract operation was made with current personnel costs at three commissaries; one each in the east, midwest and west. The current labor contracts were used for three different supermarket chains (i.e., one chain in each area). This comparison was essential to determining the potential for savings under contract operation since the supermarket chain non-personnel operating costs (such as utilities and Federal income tax) could provide little potential for savings.

(1) Following are the results of commercial contract comparisons:

<u>ITEM</u>	<u>EAST</u>		<u>MIDWEST</u>		<u>WEST</u>	
	<u>Comsy</u>	<u>Supermkt</u>	<u>Comsy</u>	<u>Supermkt</u>	<u>Comsy</u>	<u>Supermkt</u>
Number of Comparable Jobs	100	100	171	171	141	141
Average Annual Salary/Wage	\$8,462	\$10,121	\$9,622	\$11,275	\$10,728	\$13,138
Average Hourly Pay Rate	\$4.068	\$ 4.865	\$4.626	\$ 5.421	\$ 5.158	\$ 6.316
Percentage by Which Average Supermarket Chain Salary/ Wage Costs Exceed Comsy Costs		19.6%		17.2%		22.5%

NOTE: Table excludes employee benefits which, if shown, would further increase the disparity between commissary and supermarket labor costs. Civil Service benefits average 9 to 11 percent of salaries/wages compared to supermarket chains which average 20% of salaries/wages.

(2) Based on the analysis it may be assumed that for contract operation to achieve personnel costs comparable to current commissary personnel costs would require a 16% to 18% increase in productivity of contract employees (i.e., a reduction in contract employees of 16 to 18 percent from current commissary staffing levels). Since commissaries currently achieve generally higher productivity than commercial chains, largely at the expense of customer service, it is assumed a reduction of employees of this magnitude could be accomplished only by further reducing service. Notwithstanding this possibility, the operating cost estimate has been made assuming the contractor could achieve a 15 percent savings in personnel costs compared to normal supermarket chain costs.

9-4. ANALYSIS OF POTENTIAL SAVINGS.

a. Figure 1 is an estimate of operating costs which would be applicable for contract operation of commissaries based on actual results obtained by large (over \$500 million annual sales) supermarket chains during 1973 - 1974. This analysis reveals potential initial savings of 4.35 percent. Doubtful areas, such as advertising costs, were resolved in favor of contracting operations to safeguard against understating potential savings under this method of operation. Personnel costs were also reduced by 15% as previously discussed. However, there are certain unavoidable costs, such as taxes, profits and insurance, which individually are minor but collectively impact heavily on the customer savings obtainable under contract operation.

b. Results obtained from the operating costs estimate were then applied manually using the study group cost model theory to forecast operating results and sales losses. This forecast is depicted at Figure 2. A savings of about minus 1.4% and cumulative customer losses of approximately 74% were forecast under this method.

9-5. ADVANTAGES AND DISADVANTAGES OF CONTRACT OPERATION.

a. Advantages.

- (1) Contract operation would reduce Department of Defense resources required to operate a commissary system.
- (2) Could provide a wider range of items stocked for patrons.
- (3) Could provide customer service/convenience comparable to supermarkets.
- (4) Could utilize the existing distribution systems of the contractors.

b. Disadvantages.

- (1) There is a total absence of any assurance that benefits

(savings) for patrons would be obtainable at levels comparable to those of other alternatives. Strong indications exist that savings would be greatly reduced or totally eliminated.

(2) Initial major personnel turbulence due to separation, retirement, and reassignments of current Civil Service employees within the United States.

(3) Adverse morale impact on both active and retired personnel due to reduction or elimination of patron savings.

(4) It is believed that there would be a reluctance on the part of contractors to accept operation of the smaller commissaries because of disproportionate operating costs.

(5) Based on the magnitude of initial investment required, contractors would in all probability insist on a long term (minimum 5-10 years) contract to ensure ability to recoup their investments. In such a situation revocation of contracts would be feasible only under dire circumstances.

(6) Civil Service employees are not permitted to strike. Contract operation could result in actual or de facto strikes against commissaries as an adjunct to union strikes in the commercial sector. De facto strikes would occur in those situations which interrupted the distribution system of the commercial chain concerned thereby interrupting availability of stocks at commissary store level.

(7) Payment of state sales taxes on commissary purchases would be required. Rates and items taxed vary between States; however, sales taxes would increase costs to the patron by approximately 2 percent overall within the United States.

(8) Separation of wholesale procurement and distribution of resale items for commissaries from the Defense Personnel Support Center (DPSC), would increase the appropriated fund costs of that activity for troop issue. It would also reduce the capability of DPSC to perform its mission during mobilization because of reduced staffing.

(9) Continuance of the overhead structure would be required for oversea operations for which little contract competition would exist.

FIGURE 1

ANALYSIS OF SUPERMARKET CHAIN OPERATING COSTS (FIRMS
WITH ANNUAL SALES ABOVE \$500 MILLION) APPLICABLE FOR
CONTRACT OPERATION

	<u>1973-1974 Operating Costs (Margin Basis)</u>	<u>Applicable for Contract Operation of Commissaries</u>	<u>% Applicable for Contract Operation of Commissaries</u>	<u>Remarks</u>
<u>Payroll salaries and Benefits</u>	11.59	YES	9.85	Note 1
<u>Supplies (Consumable Supplies, Including Office)</u>	.96	YES	.96	
<u>Utilities (All Utilities Except Telephone)</u>	.81	YES	.81	
<u>Communications</u>				
Postage, Telephone Toll Service, Telegrams, Cables, etc.	.09	YES	.09	
<u>Travel</u>	.10	YES	.10	
<u>Services Purchased</u>				
Advertising, Hired Hauling, Laundry, Pest Control, Sanitation, Armored Service, etc.	1.32	YES Except Advertising	.46	Note 2
<u>Promotional Activities</u>				
Trading Stamps, Premiums, Certificates, & Coupons	.76	NO	-0-	
<u>Professional Services</u>				
Accountants, Lawyers, appraisers, Architects, etc.	.05	YES	.05	
<u>Donations</u>				
Self-Explanatory	.01	NO	-0-	
<u>Insurance Purchased or Self-insured</u>	.71	YES	.71	
<u>Taxes and Licenses</u>				
State, Local License Fees -not income-	1.02	YES	1.02	
<u>Property Rentals</u>				
Real Estate	1.38	YES	.0	Note 3

FIGURE 1 (Continued)

	<u>1973-1974 Operating Costs (Margin Basis)</u>	<u>Applicable for Contract Operation of Commissaries</u>	<u>% Applicable for Contract Operation of Commissaries</u>	<u>Remarks</u>
<u>Equipment Rentals</u> Cash registers, computers, accounting machines, trucks, etc.	.10	YES	.10	
<u>Depreciation and Amortization</u> Buildings and Equipment	.77	YES	1.17	Note 3
<u>Repairs</u> Maintenance by others of Bldgs and equipment	.63	YES	.63	
<u>Miscellaneous</u>	.80	YES	.80	
<u>Income Tax</u>	.54	YES	.54	
<u>Profit</u> (Net earnings after income tax)	.57	YES	.57	
TOTAL	22.21		17.86	

Note 1 - Assumes contractor achieves a 15% decrease in personnel costs based on higher average commissary sales volumes and associated factors.

Note 2 - Advertising deducted on assumption contractor would not allocate this cost to commissaries.

Note 3 - Assumes contractor would not pay for land use or leasing of commissary facilities but would have construction and equipment purchase costs. Items adjusted accordingly to levels required under in-house alternatives.

	<u>As % of Contract Selling Prices</u>	<u>As % of Equivalent Supermarket Prices</u>
<u>Cost of Goods Sold</u>	81.328	77.79
<u>Operating Costs</u>	18.672	17.86
Initial % Savings (Before Patron Loss)		4.35
TOTAL	100.00	100.00

Source: 1973-1974 Operating Costs - "Operating Results of Food Chains 1973-1974",
Cornell University

FIGURE 2

ECONOMIC IMPACT AND COST COMPARISON BY MILITARY
SERVICE OF SELECTED ALTERNATIVES
CONTRACT OPERATION

Alternative #4

Low Sales Loss - Low Curve

Assumed Initial Savings	%	22.0%
Assumed Incremental Sales Loss	%	41%
Equivalent Supermarket Sales	\$ m	\$1,489.5
Estimated Commissary Sales	\$ m	\$1,510.4
Costs:		
Cost of Goods Sold (CGS)	\$ m	\$1,158.9
Cost of Goods Sold	% Sales	76.7%
Personnel	\$ m	\$ 146.8
Personnel	% Sales	9.7%
Operations	\$ m	\$ 174.4
Operations	% Sales	11.5%
Capital Outlay	\$ m	\$ 30.3
Capital Outlay	% Sales	2.0%
Total Costs (Less CGS)	\$ m	\$ 351.5
Total Costs (Less CGS)	% Sales	23.3%
Expected Incremental		
Sales Loss	%	33
Expected Savings	%	- 1.4
Expected Total Sales Loss	%	74

NOTE: Results are depicted for the iteration at which it became no longer worthwhile to continue analysis to determine a final outcome for this alternative. At this point savings and sales losses rendered further iterations unnecessary.

CHAPTER 10

CIVIL SERVICE PERSONNEL CONSIDERATIONS

10-1. BACKGROUND. Military commissary stores employ about 25,000 civilian employees, of whom slightly more than 3,000 are foreign nationals working in stores overseas. Little personnel impact on most foreign national employees would result if commissary store operations were shifted to employment in a nonappropriated fund mode. Therefore, personnel considerations during this study have concentrated upon assessing the impact of proposed actions upon U. S. citizen civilian employees and examining the ways in which cost savings might be obtained through adaptation of personnel practices common to large supermarket chain operations.

10-2. CIVIL SERVICE VS NAF EMPLOYMENT.

a. In view of the requirement for commissaries to recover the costs of direct labor, continuing to operate with a Civil Service work force was evaluated. Operation of commissary stores with a nonappropriated funded (NAF) work force would present certain advantages; predominantly in the areas of hiring, promotion and scheduling flexibility. However, serious immediate disadvantages could result from a sudden shift to NAF employment. A shift to NAF employment:

(1) would incur significant one-time costs to pay employees for their accrued annual leave (generally referred to as terminal leave costs);

(2) could also generate substantial severance pay costs;

(3) could result in considerable personnel turbulence, and

(4) substantial portions of the work force could be lost through retirement or reassignment to other Civil Service jobs.

b. The present work force is competent, motivated, and, by usual commercial supermarket measurement standards, more productive than their counterparts in the private sector. The next several years are crucial to the future of the commissary store system. Major changes in organization and operation are required to improve efficiency. It is essential that employees - especially key managers - be retained to prevent a deterioration of service that would inevitably cause large losses in sales and customers. Therefore, it is inadvisable at this time to consider any shift to NAF employment.

10-3. SEVERANCE PAY AND TERMINAL LEAVE COST IMPLICATIONS.

a. General. A detailed analysis was made of the present U. S. citizen civilian work force to estimate the potential costs that would

be incurred if it became necessary to pay employees severance pay and accrued annual leave. The analysis identified all U. S. citizen civilian employees paid from appropriated funds who are directly assigned more than half their time to commissary resale functions. Data used was extracted from the U. S. Civil Service Commission central personnel data file and matched against a computer program. The computer program produced summary data about retirement coverage and eligibility for immediate annuity, severance pay costs, current average wage and insurance costs, and present work schedules for both permanent and temporary employees. Summaries of these data are contained in Volume II, Appendices 10-A and 10-B.

b. Severance Pay. Under a government-owned, contractor operated commissary system as envisioned by Alternative 4, full severance pay liability would be incurred. Similarly, conversion of employees to nonappropriated fund employment as proposed under Alternative 2 (merging commissary systems with existing exchange systems) would entail severance pay if employees were not given continuing employment or refused offers of employment that were less than comparable with their present positions. Based upon Federal Personnel Manual criteria, the present salaries, ages, and service of eligible employees, total severance pay cost, as of 1 October 1976, is estimated to be a maximum of \$54 million. A breakdown of this cost by military component is contained in Volume II, Appendix 10-A, Figure 1, Part 2.

c. Terminal Leave. Any condition which would terminate appropriated fund Civil Service employment would incur terminal leave costs for all employees except those who are employed on an intermittent basis. To estimate what these costs would be, calculations were made for an extrapolated workforce of 21,980 employees. Temporary employees were presumed to be eligible for payment on an average leave balance of 80 hours, and career or career-conditional employees were estimated to be eligible for payment on an average balance of 240 hours accrued annual leave. This last figure was arrived at by adding 80 hours to a total of 160 hours which was determined to approximate the present average leave balance for a sample of almost 70,000 DOD civilian employees serviced by four Department of Army payroll offices. The 80 additional hours were added on the assumption that long advance notice would be given and that employees would generally forego using annual leave in order to maximize their terminal leave payment. The potential terminal leave cost is estimated to be in excess of \$20 million dollars. A further breakdown of this cost by military component is contained in Volume II, Appendix 10-A, Figure 1, Part 2.

10-4. EMPLOYEE PERSONNEL COSTS AND DISTRIBUTION BY WORK SCHEDULE.

a. General. Commercial supermarkets employ a greater percentage of their workforce on an other-than-full-time basis than do commissaries, partly because it is more economical in terms of fringe benefits. These benefits range from 20 to as much as 50 percent of basic hourly wages. Also,

employees working on part-time or intermittent bases can be hired to meet the labor needs of heavy workload periods without also incurring correspondingly high costs during periods of light customer shopping. Estimates indicate that large supermarket chains employ approximately 60 percent of their workforce on a full-time basis.

b. Present Salary Costs. The report previously mentioned provided data that could be used to estimate the current salary costs for full-time employees and, on a man-year equivalent basis, for employees now working on part-time and intermittent work schedules. Raw wages were adjusted to reflect the difference in fringe benefits accorded to career and career-conditional employees receiving Civil Service retirement coverage and the full range of other benefits and intermittent employees who incur only FICA (social security) and workman's compensation costs. Figure 1 of Appendix 10-C shows these costs by each military component. Generally, on a man-year equivalent basis, intermittent employees are less costly than are part-time employees; however, they are more costly in the Army which uses almost three times as many intermittent employees as part-timers and in higher paying jobs. Estimated total annual costs were computed on the basis of a work force of 21,980 employees.

c. Current Employee Mix. Currently, 89% of all service commissary store employees are full-time. This ranges, however, from 99% in the Marine Corps to 71% in the Navy. Figure 1, Appendix 10-C shows the composition of the various work forces by work schedule and relationship to present labor costs.

10-5. POTENTIAL SAVINGS IN PERSONNEL COSTS THROUGH INCREASED USE OF OTHER THAN FULL-TIME EMPLOYEES.

a. General. To analyze the potential for savings in personnel costs for U. S. citizen civilian employees, a cost model was constructed which used present man year salary levels (including applicable benefits). The model was used to calculate total salary costs as the percentage of other than full-time employees was increased from the present compositions to an ultimate ratio of 60 percent full-time and 40 percent other than full-time. Preliminary trials of the model established that the proportion of part-time to intermittent employees was not as significant a factor in the outcome of savings as was a decrease in the percentage of full-time employees. The results of this analysis (Figure 1, Appendix 10-D) show savings of more than \$10 million dollars are possible if the other three services merely duplicate the Navy's present work force configuration and that more than \$15 million dollars in savings are possible if each service reaches a proportion of 60 percent/40 percent. Expressed as a percentage, this constitutes a reduction of more than 7 percent in overall personnel costs.

b. Achieving a Better Mix. Transition from the present work schedule to a more cost-effective configuration that would better match work force to workload is intended to be achieved through attrition due to normal turnover.

This will permit a conversion to be accomplished without adverse effect upon present employees, thereby eliminating severance costs and avoiding lowered employee morale.

c. Difficulties Experienced. The Navy has not reached its present work force mix without encountering some difficulties that result from the inability of present competitive procedures to respond quickly to the special labor needs of commissary stores. First, present Civil Service Commission examination and announcement practices are not generally viewed by job applicants as a means of obtaining other than full-time employment. As a result, normal appointment certificates produce few applicants willing to accept such job offers and those who do often use it as a "springboard" to secure full-time competitive employment through subsequent non-competitive conversion to positions with full-time work schedules. In a sense, such employees are thwarting the "selection in order" concept of competitive appointment procedures, as well as creating an unduly heavy recruiting workload to replace them when they "back door" themselves into full-time jobs through merit selection procedures. Use of temporary appointment authorities is not the answer to this problem because it further restricts the number of interested applicants and creates the necessity for eventually terminating employees who may turn out to be highly desirable.

d. Changes Needed. Several possible solutions to these difficulties exist. These include:

(a) use of appointment registers that are drawn up specifically for the purpose of offering less than full-time employment,

(b) use of special Schedule A appointment authority that would limit the privilege of conversion to full-time competitive appointment,

(c) redesignation of certain commissary store functions to a Service type concept to permit more flexible scheduling authority.

10-6. REDUCTION-IN-FORCE IMPLICATIONS.

Each of the four alternatives involves some adverse action and reduction-in-force implications. As has been previously mentioned, merging with existing exchange systems or operation under a Government owned, contractor operated (GOCO) arrangement would present the most severe conditions. Adverse impact upon employees outside of the commissary store organization may be minimized in the exchange system consolidation by treating it as a transfer of function action. Establishment of centralized separate service commissary systems would cause some personnel turbulence as a result of functional consolidations. To a greater degree the same would be true for establishment of a Joint Service Commissary Agency.

10-7. END STRENGTH RESTRICTIONS. Since the customer will be supporting labor cost for civilian employees, end-strength restrictions will not serve to limit cost to appropriations. These restrictions unduly inhibit effective management of the commissary labor force. The law now requires ceilings to apply equally to permanent or temporary, full-time, part-time, or intermittent employees. This forces commissaries to use an excess of more costly full-time personnel to stay within ceilings when use of other than full-time employees would reduce cost. It also involves the commissaries in command imposed hiring freezes, etc., which cause such poor management practices as being substantially understrength at peak sales periods.

10-8. TRAINING AND CAREER DEVELOPMENT.

a. General. Formal training opportunities in the management and operation of military commissary stores are limited. The Navy provides centralized managerial and functional training in meat market operations although most of their management positions are filled by military personnel. The Army has been providing central training in general commissary store management and in the technical functions of meat, produce, grocery and store operations. The Army technical functional courses are being discontinued at the end of FY 1975. The Navy and the Army also offer extension or correspondence training courses in all aspects of commissary operations. The Air Force and Marine Corps utilize the training opportunities available from the Army and Navy. All of the military services provide on-the-job training and participate in installation training courses in supervision, management and labor relations conducted by civilian personnel offices.

b. Training Needs. The changes to be implemented within the military commissary system require highly qualified, well-trained personnel to achieve the most efficient, economical operations possible. There is a need for the services to provide additional training opportunities, particularly in commissary management and the specialized functional areas such as meat and produce processing and warehousing. The specialized training can best be provided in the classroom atmosphere rather than through extension courses. The possibility exists that standard training units could be developed for specific functions which would satisfy the requirements of all the military services.

c. Improving career opportunities. Long range operating economies in the commissary store systems are possible when management positions are occupied by a cadre of qualified civilians who are willing to make a career in the commissary store system. To accomplish this end, an intern development program must be designed and placed into operation. Formal training at a centralized location covering standard aspects of management and operations may be made more effective through joint service administration. For best results, recruitment of interns must be done on a regular, planned basis. Selectees may come from within present work forces or from intern registers, but execution of mobility agreements is essential in order that well-rounded training can be designed and management can ensure that the system benefits from the substantial investment made. Centralization of commissary store management will broaden the opportunities for expanding career horizons.

CHAPTER 11

LEGAL AND LEGISLATIVE CONSIDERATIONS

NOTE: Legislation is referred to in this Chapter by United States Code title and section, i.e., 10 U.S.C. 125; or by the year, subject, and public law number in the case of annual appropriation and authorization acts. For ready reference, the U.S. Code text of the more significant legislation is contained in Appendix 11-A and referred to in this chapter.

11-1 BACKGROUND-EXISTING LEGISLATION

a. General.

The legislation directly affecting military commissaries consist principally of the laws authorizing commissary sales by the military departments (10 U.S.C. 4621, Army; 7601-7605, Navy; and 9621, Air Force: Appendix 11-A, pages 11-10 through 11-14) and the annual Defense Appropriations Acts which, since 1952, have forbidden the use of appropriated funds to pay certain commissary cost (Current text, Appendix 11-A, page 11-17). There is also a law authorizing private persons to operate commissary stores, (10 U.S.C. 2482: Appendix 11-A, page 11-15) and a 1974 law permitting adjustments or surcharges on commissary sales to provide funds for construction and related costs (10 U.S.C. 2685, Appendix 11-A, page 11-16).

While not legislation, as such, the House Armed Services Committee must approve basic organizational and operating regulations for military commissaries and exchanges before they are implemented. This control is not established by a specific law but is legislative oversight exercised by the Committee under its authority to conduct inquiries and investigations relative to its legislative function (See page 12885, H.A.S.C. Rep. No. 91-81, 2nd Sess., 1970). There are separate DOD Directives published under this Congressional oversight for commissaries (DOD Directive 1330.17, October 29, 1971, Subject: Armed Services Commissary Store Regulations) and exchanges (DOD Directive 1330.9, October 29, 1971, Subject: Armed Services Exchange Regulations).

b. Basic Authorizing Laws.

The Army and Air Force authorizations are practically identical, having their origins in an 1866 Act of Congress. The Navy Department authorization, which includes the Marine

Corps, originated in a 1909 Act. The terminology differs, with the Navy law using the word "stores", which has been interpreted to include commissary stores. The Army-Air Force law authorizes sale of "subsistence supplies". Interestingly, the word "commissary" is not used in either basic authorization and only appears once in a section authorizing Navy "commissary" officers overseas to accept checks. In each of the authorizations the wording is permissive, i.e.:... "stores ... may be...sold..." (Navy), and "Subsistence Supplies may be sold ..." (Army-Air Force). A significant difference in the two authorizations is the requirement that the Army-Air Force sell each article at invoice cost; there being no similar requirement for the Naval Services.

c. The following paragraphs will discuss the impact of existing legislation and new legislative requirements for the four alternatives discussed in this study report. There are four crucial changes that are required under all alternatives, and they will be considered first.

11-2. LEGISLATIVE CHANGES REQUIRED BY ALL ALTERNATIVES STUDIED

a. General

Each alternative includes the new requirement of Program Budget Decision (PBD) 282 for the customer to pay for direct personnel cost and overseas utilities. In light of these additional costs, there are four changes to current legislation that are needed regardless of the alternative - or combination of alternatives - selected. They are:

b. Variable Pricing.

The use of varying markups is the universal practice of the retail industry. In the civilian grocery sector this ranges from selling below cost to a widely varying percentage of markups above cost. In general the basic necessities (milk, bread, etc.) enjoy a low markup, and slower moving convenience items, a higher markup. As the commissary system absorbs additional cost, this will mean that our necessities, if sold at invoice cost plus a flat surcharge, will cost more in a commissary than in a civilian store, while less essential items will sell much below civilian store prices. This would not only be inequitable, but would cause a great loss of patronage to the commissaries. To prevent this, it is necessary to delete the sentence in 10 U.S.C. 4621 (b) and 9621 (b) (Appendix 11-A, pages 11-10 and 11-12) which requires the Army and Air Force to sell each item at invoice cost. This requirement has already been fractured by the Annual Appropriation Act and the Commissary Construction Act, and should now be laid to rest. This

change is absolutely necessary for the continuation of commissaries under the requirements of PBD 282.

c. End Strength Restrictions

Section 501 of the Defense Appropriation Authorization Act (P.L. 93-365, Appendix 11-A, pages 11-18 and 11-19) contains end strengths for civilian personnel for each military department. Subsection (b) tells how to compute end strengths and excludes certain special categories of employees from end strength requirements. Since PBD 282 requires that markups paid by the customer be used to pay the cost of personnel working in commissary systems, it seems appropriate that such employees be excluded from end strength restrictions. End strength restrictions prevent achieving a higher proportion of other than full-time employees, thus causing overall higher personnel costs. These restrictions have hampered the effective management of commissary stores in the past and would be repugnant to a more self-supporting commissary operation.

d. Authority to Invest Surcharge Funds

The trust funds generated from markup or surcharge will be much larger than before since they must be increased to pay the additional cost. This will be particularly noted as surcharge collections are used to build up construction funds under 10 U.S.C. 2685 and pay personnel cost. Short and long term investment of these customer generated funds is essential for a more self-supporting and business-like commissary system. It can be argued that legislation is not required to permit investment of surcharge funds since they do not come from direct appropriations and since non-appropriated fund entities, e.g. the Army and Air Force Exchange Service, do invest funds. However, a more careful appraisal supports the view that surcharge funds are essentially different from Exchange Service funds. While surcharge comes directly from the customer, it is derived as an incident to the sale of commissary items which are purchased from an appropriated source (stock fund). Surcharge funds are specifically authorized by law (Construction Act and Annual Appropriations Act, Appendix 11-A, pages 11-16 and 11-17) and are required by the Appropriations Act to be used to make reimbursements to appropriated funds. These factors support a conclusion that they are subject to the statutory prohibitions against expending (investing) government funds without legislative authority (see 31 U.S.C. 628, 665). Legislative authority for the Treasury to invest government trust funds in securities of the United States, are not uncommon (see 10 U.S.C. 2601, General Gift Funds; 10 U.S.C. 6973 c, Naval Academy Gift Fund; 46 U.S.C. 1272 Federal Ship Finances Fund). Legislative authority is

necessary, and should be obtained, to permit commissary surcharge funds to be similarly invested.

e. Remove Distance Price and Adequacy Criteria From Annual Appropriations Act. The basic statutory authorities do not impose any criteria for the operation of commissary stores (see Appendix 11-A, page 11-10 through page 11-14). However, the last sentence of the commissary section of the Annual Defense Appropriations Acts has, since 1954, stated that no appropriation contained therein shall be available in connection with the operation of commissary stores within the Continental United States unless the Secretary of Defense certifies that items are not otherwise available (1) at a reasonable distance, (2) at a reasonable price and (3) in satisfactory quality and quantity, (Appendix 11-A, page 11-17). This provision has been enacted annually to control the expenditure of appropriated funds. The implementation of PBD 282 will virtually eliminate the direct use of appropriated funds "in connection with the operation of commissary stores within the Continental United States" and, depending on the interpretation of those words, it could be said that the Secretary of Defense will no longer be required to make such certifications. However, to remove any doubt, it is necessary to omit this last sentence from future appropriation acts. This would permit the service secretaries to determine the location of commissary stores under their basic authority.

11-3. CREATION OF CENTRALIZED COMMISSARY SYSTEMS IN THE SEPARATE SERVICES. The existing legislative authority for the three departments to operate commissaries (Appendix 11-A, pages 11-10 to 14) and the stock fund authority (10 U.S.C. 2208, Appendix 11-A, pages 11-21 and 11-22) are sufficiently broad to allow the secretaries to realign current systems without additional legislation. However the change to allow variable pricing for the Army and Air Force (see discussion in paragraph 11-2 b) would be necessary, and the other three changes (relief from end strengths, reinvestment of surcharge and removal of criteria) highly desirable (discussion, paragraph 11-2 c, d, and e).

11-4. CONSOLIDATION OF COMMISSARY SYSTEMS WITH EXISTING EXCHANGE SYSTEMS.

a. General. Service commissary stores could be merged into their respective exchange system without enabling legislation. There are, however, a number of problem areas which may require legislation for resolution. It is important to recognize the historic differences between the commissary and exchange systems and the way these historic differences have been reflected in the attitude of Congress.

b. Commissary Stores. There is specific statutory authority for each of the military departments to operate commissary stores (Appendix 11-A, pages 11-10 to 14). In the case of the Army and Air Force, this authority specifically allows appropriated funds to be used for the purchase of subsistence supplies for resale (see subsection (1), pages 11-11 and 11-13, Appendix 11-A).

There is no general prohibition on the use of appropriated funds to support commissaries; the Annual Appropriations Act lists only specific items which appropriated funds cannot support (Appendix 11-A, page 11-17).

c. Exchanges

Conversely, there is no specific statutory authority for the existence of any of the service exchange systems, although there is legislation which affects them. They are creatures of, and largely operated under, regulations issued by the services. The authority to issue these regulations derives from the general powers granted by Congress to the respective service secretaries to administer their departments (see 10 U.S.C., Sections 3012, Army; 5031, Navy; and 8012, Air Force). In the case of the Army and Air Force there is a specific statutory prohibition against spending appropriated funds to support exchanges, with the exception of public buildings and transportation not needed for other purposes (10 U.S.C. 4779, Army; 9779, Air Force; Appendix 11-A, page 11-20).

d. Problem Areas

(1). Working Capital Funds. Working Capital Funds (stock funds), organized under 10 U.S.C. 2208 (Appendix 11-A, pages 11-21 and 11-22) are used to support commissaries. Each service uses such a fund to purchase inventory, and the Defense Personnel Support Center (DPSC) uses stock funds to support its activities. A direct transfer of commissary inventories to the exchange services, without reimbursement, would seem to violate the general requirement of 10 U.S.C. Section 2208 h (Appendix 11-A, page 11-22), that the stock funds must be "re-imbursed for supplies so sold" (see also 31 U.S.C. 686 requiring payment if government property is transferred between government entities and 31 U.S.C. 483a for transfers to a non-government entity). Also, a non-reimbursed transfer might violate 10 U.S.C. 4779 and 9779 prohibiting use of appropriated funds to support exchanges. The two possible alternatives are: (1) have the exchanges pay for the inventories or (2) transfer possession, but not title, of the inventories to the exchange and allow use of the proceeds to replenish the inventory, which would always be accounted for separately, so possession could be returned, if necessary. Since the cost of purchasing the inventory is impractical, the second alternative seems the only logical one. In effect, the exchanges would be acting as the agent of the service secretaries to carry out their statutory authority to sell commissary items. This theory would also seem to remove the obstacle of using DPSC stock funds to support purchases. However, Exchange operation of commissaries would have to be segregated and "profits" could not be used to support welfare programs, without legislative authority.

(2). Employees. The impact of changing employees to a non-appropriated status is treated extensively in Chapters 7 and 10. The statutes most directly involved are 5 U.S.C. 5102c(14) which specifically excludes non-appropriated fund employees from the provisions of the Civil Service Classification Act, and 5 U.S.C. 2105(c) which states that non-appropriated fund employees are not considered employees of the United States for the purpose of any laws administered by the Civil Service Commission or the Federal Employees Compensation Act. However, the Henderson Act (10 U.S.C. 5342(a)(2)) includes non-appropriated employees as employees for whom prevailing wage rate determinations are required, but such determinations have different ground rules from Civil Service employees. Provisions of 5 U.S.C. 5595 govern the entitlement of Civil Service employees to severance pay. Implementing Civil Service regulations provide that an employee is not entitled to severance pay if he is offered comparable employment with a Federal instrumentality to which his activity is transferred. (See 5 C.F.R., Section 550.701(b)(7)). A Court of Claims decision has interpreted the meaning of "comparable employment" (Mark M. Atkins et. al. v. The United States, 439 F. 2d 175; 194 Ct. Cl. 477(1971)).

11-5 CREATION OF A JOINT SERVICE AGENCY TO OPERATE ALL COMMISSARY STORES

a. Authority for Defense Reorganizations. The Defense Reorganization Act of 1958 granted the Secretary of Defense the authority to reassign, transfer, abolish, or consolidate any function to provide more effective, efficient, and economical administration and operation, and to eliminate duplication. A function vested by law may not be consolidated under this Act until the Secretary reports to Congress and 30 days elapse while Congress is in continuous session (10 U.S.C. 125, Appendix 11-A, pages 11-23 and 11-24). There are further provisions permitting the transfer of appropriations upon approval of the President (which was delegated to the Director of OMB by Executive Order 11230, June 1965, 30 FR 8447) and the transfer of civilian personnel upon approval of the Director of the Office of Management and Budget (10 U.S.C. 126). Also, the stock fund law (Appendix 11-A, pages 11-21 and 11-22) now used to purchase inventories for commissaries, gives the Department of Defense broad latitude in handling such funds.

b. Reorganization of Commissaries Would Not Require New Laws. Under these authorities there seems to be no requirement for new legislation to consolidate the existing commissary systems into a unified joint service agency or to make re-alignments among or between current systems. A report to Congress would evidently be required by 10 U.S.C. 125 since the current service operation of commissaries is vested -- even though permissibly -- by law.

11-6. GOVERNMENT OWNED - CONTRACTOR OPERATED

a. General.

It is difficult to assess new legislative requirements, or the impact of existing laws, for this alternative since the alternative has not been attractive enough to prepare detailed specifications for potential bids. The degree to which potential contractors control personnel, inventory, pricing, purchasing, distribution, etc. would affect new legislative requirements and be affected by existing law. Because of the many variables involved no attempt is made to discuss all the possibilities. The following are areas of concern under any contractual arrangement:

b. State Sales and Use Tax.

About half of the states impose sales taxes on food. Commissary stores do not collect such taxes now since they are Federal entities. A contractor operated store would probably be subject to these taxes under most modes of operation. The fact that operation would be on a Federal area affords no relief since Congress has expressly sanctioned imposition of state taxes within Federal areas. (4 U.S.C. 105, Appendix 11-A, page 11-25.)

c. Duration of Contract.

It is assumed that any contractual arrangement would have to depend on appropriated funds as a primary source (or at least a guarantor) even though the appropriated funds would be partially or totally reimbursed by markups on sales. Therefore, the contracts would be dependent on Congressional appropriations and necessarily limited in duration. The Anti-Deficiency Act (31 U.S.C. 665 (a)) prohibits involving the Government in any contract or other obligation in advance of appropriations. Appropriations for operation and maintenance are normally made for one year at a time. While there are laws permitting multi-year contracting they are tightly prescribed. (See e.g. 10 U.S.C. 2306 (g) and Armed Service Procurement Regulation (A.S.P.R.) 1-322). These limitations would have a definite impact on price and terms of any contractual arrangement. If the contractor were expected to build up personnel, distributing capacity, etc., he would naturally

require a long-term commitment or his quoted price must be very high to cover such cost without normal amortization.

d. Use of Stock Fund.

The stock fund law permits supplies to be sold to or services to be rendered or work performed for persons outside the Department of Defense where it is otherwise authorized by law. (10 U.S.C. 2208 (h) Appendix 11-A, page 11-22. If a private contractor were to be considered an independent entity and, thus, a person outside the Department of Defense, use of the stock fund would seem to be prohibited. This would depend on the type of contractual arrangement involved and might be avoided by a more limited service-type contract.

e. Limitations on Service Contracts.

A service contract is one which calls directly for a contractor's time and effort rather than for a concrete end product (A.S.P.R. 22.101 (a)). The procurement of services by means of contract has been the subject of much concern by Congress, the Civil Service Commission, the Comptroller General and the Department of Defense. Basically, it is forbidden to circumvent Civil Service laws and regulations, the Classification Act and personnel ceilings by procuring contractual service in such a manner that the contractor or his employees are, in effect, employees of the Government. (A.S.P.R. 22.102.1). A determination on this question would depend on the details of the contractual arrangement.

APPENDIX A
CHAPTER 11

EXISTING LEGISLATION

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ARMY AUTHORIZATION
10 USC 4621

Section 4621. Quartermaster supplies: members of armed forces; veterans; executive or military departments and employees; prices.

(a) The branch, office, or officer designated by the Secretary of the Army shall procure and sell, for cash or credit--

(1) articles specified by the Secretary of the Army or a person designated by him, to members of the Army; and

(2) items of individual clothing and equipment, to officers of the Army, under such restrictions as the Secretary may proscribe. (Sic)

An account of sales on credit shall be kept and the amount due reported to any branch, office, or officer designated by the Secretary. Except for articles and items acquired through the use of working capital funds under section 2208 of this title, sales of articles shall be at cost, and sales of individual clothing and equipment shall be at average current prices, including overhead, as determined by the Secretary.

(b) Subsistence supplies may be sold to members of the Army. The selling price of each article sold under this subsection is the invoice price of the last lot of that article that the officer making the sale received before the first day of the month in which the sale is made. Activities conducted under this subsection shall be consistent with section 2208 of this title.

(c) The branch, office, or officer designated by the Secretary shall sell subsistence supplies to members of other armed forces at the prices at which like property is sold to members of the Army.

(d) The branch, office, or officer designated by the Secretary may sell serviceable quartermaster property, other than subsistence supplies, to an officer of another armed force for his use in the service, in the same manner as these articles are sold to an officer of the Army.

(e) A person who has been discharged honorably or under honorable conditions from the Army, Navy, Air Force, or Marine Corps and who is receiving care and medical treatment from the Public Health Service or the Veterans' Administration may buy subsistence supplies and other supplies, except articles of uniform, at the prices at which like property is sold to a member of the Army.

(f) *****

(g) Whenever, under regulations to be prescribed by the Secretary, subsistence supplies are furnished to any branch of the Army or sold to employees of any executive department other than the Department of Defense, payment shall be made in cash.

(h) The Secretary may, by regulation, provide for the procurement and sale of stores designated by him to such civilian officers and employees of the United States, and such other persons, as he considers proper--

(1) at military installations outside the United States; and

(2) at military installations inside the United States where he determines that it is impracticable for those civilian officers, employees, and persons to obtain those stores from private agencies without impairing the efficient operation of military activities.

However, sales to officers and employees inside the United States may be made only to those residing within military installations.

(i) Appropriations for subsistence of the Army may be applied to the purchase of subsistence supplies for sale to members of the Army on active duty for the use of themselves and their families.

AIR FORCE AUTHORIZATION
10 USC 9621

Section 9621. Subsistence and other supplies: members of armed forces; veterans; executive or military departments and employees; prices.

(a) The Secretary of the Air Force shall procure and sell, for cash or credit--

(1) articles designated by him, to members of the Air Force, under such restrictions as the Secretary may prescribe.

An account of sales on credit shall be kept and the amount due reported to the Secretary. Except for articles and items acquired through the use of working capital funds under section 2208 of this title, sales of articles shall be at cost, and sales of individual clothing and equipment shall be at average current prices, including overhead, as determined by the Secretary.

(b) Subsistence supplies may be sold to members of the Air Force. The selling price of each article sold under this subsection is the invoice price of the last lot of that article that the officer making the sale received before the first day of the month in which the sale is made. Activities conducted under this subsection shall be consistent with section 2208 of this title.

(c) The Air Force shall sell subsistence supplies to members of other armed forces at the prices at which like property is sold to members of the Air Force.

(d) The Secretary may sell serviceable quartermaster property, other than subsistence supplies, to an officer of another armed force for his use in the service, in the same manner as these articles are sold to an officer of the Air Force.

(e) A person who has been discharged honorably or under honorable conditions from the Army, Navy, Air Force, or Marine Corps and who is receiving care and medical treatment from the Public Health Service or the Veterans' Administration may buy subsistence supplies and other supplies, except articles of uniform, at the prices at which like property is sold to a member of the Air Force.

(f) *****

(g) Whenever, under regulations to be prescribed by the Secretary, subsistence supplies are furnished to any organization of the Air Force or sold to employees of any executive department other than the Department of Defense, payment shall be made in cash.

(h) The Secretary may, by regulation, provide for the procurement and sale of stores designated by him to such civilian officers and employees of the United States, and such other persons, as he considers proper--

(1) at military installations outside the United States; and

(2) at military installations inside the United States where he determines that it is impracticable for those civilian officers, employees, and persons to obtain those stores from private agencies without impairing the efficient operation of military activities.

However, sales to those officers and employees inside the United States may be made only to those residing within military installations.

(i) Appropriations for subsistence of the Air Force may be applied to the purchase of subsistence supplies for sale to members of the Air Force on active duty for the use of themselves and their families.

NAVY AUTHORIZATION
10 USC 7601-7603 & 7605

Section 7601. Sales: members of naval service and Coast Guard; widows; civilian employees and other persons

(a) Such stores as the Secretary of the Navy designates may be procured and sold to members of the naval service, members of the Coast Guard, and widows of such members.

(b) The Secretary may, by regulation, provide for the procurement and sale of stores designated by him to such civilian officers and employees of the United States, and such other persons, as he considers proper--

(1) at military installations outside the United States; and

(2) at military installations inside the United States where he determines that it is impracticable for those civilian officers, employees, and persons to obtain those stores from private agencies without impairing the efficient operation of naval activities.

However, sales to civilian officers and employees inside the United States may be made only to those residing within military installations.

Section 7602. Sales: members of Army and Air Force; price

The Navy and the Marine Corps shall sell subsistence supplies to any member of the Army or the Air Force at prices charged members of the Naval service.

Section 7603. Sales: veterans under treatment

A person who has been separated honorably or under honorable conditions from the Army, the Navy, the Air Force, or the Marine Corps and who is receiving care and medical treatment from the Public Health Service or the Veterans' Administration may buy subsistence supplies and other supplies, except articles of uniform, from the Navy and the Marine Corps at prices charged members of the naval service.

Section 7605. Acceptance of Government checks outside the United States

Notwithstanding sections 521 and 543 of title 31, the Secretary of the Navy may authorize the officer in charge of any commissary store or ship's store ashore located outside the United States to--

(1) accept any Government check tendered by a retired member of the Navy or the Marine Corps, a member of the Naval Reserve or the Marine Corps Reserve, or a member of the Fleet Reserve or the Fleet Marine Corps Reserve, if the member is the payee of the check and the check is tendered in payment of amounts due from the member to the store; and

(2) refund in cash any difference between the amount due and the amount of the tendered check.

PRIVATE PERSONS
10 USC 2482

Section 2482. Commissary stores: private operation

Private persons may operate commissary stores under such regulations as the Secretary of Defense may approve.

CONSTRUCTION SURCHARGE
10 USC 2685

Section 2685. Adjustment of or surcharge on selling prices in commissary stores to provide funds for construction and improvement of commissary store facilities.

(a) Notwithstanding any other provision of law, the Secretary of a military department, under regulations established by him and approved by the Secretary of Defense, may, for the purposes of this section, provide for an adjustment of, or surcharge on, sales prices of goods and services sold in commissary store facilities.

(b) The Secretary of a military department, under regulations established by him and approved by the Secretary of Defense, may use the proceeds from the adjustments or surcharges authorized by subsection (a) to acquire, construct, convert, expand, install, or otherwise improve commissary store facilities at defense installations within the United States and for related environmental evaluation and construction costs, including surveys, administration, overhead, planning, and design.

CURRENT SECTION 814 OF THE GENERAL PROVISIONS
OF THE DOD APPROPRIATIONS ACT - PL 93-437

Section 814. No appropriation contained in this Act shall be available in connection with the operation of commissary stores of the agencies of the Department of Defense for the cost of purchase (including commercial transportation in the United States to the place of sale but excluding all transportation outside the United States) and maintenance of operating equipment and supplies, and for the actual or estimated cost of utilities as may be furnished by the Government and of shrinkage, spoilage, and pilferage of merchandise under the control of such commissary stores, except as authorized under regulations promulgated by the Secretaries of the military departments concerned with the approval of the Secretary of Defense, which regulations shall provide for reimbursement therefor to the appropriations concerned and, notwithstanding any other provision of law, shall provide for the adjustment of the sales prices in such commissary stores to the extent necessary to furnish sufficient gross revenue from sales of commissary stores to make such reimbursement: Provided, That under such regulations as may be issued pursuant to this section all utilities may be furnished without cost to the commissary stores outside the continental United States and in Alaska: Provided further, That no appropriation contained in this Act shall be available in connection with the operation of commissary stores within the continental United States unless the Secretary of Defense has certified that items normally procured from commissary stores are not otherwise available at a reasonable distance and a reasonable price in satisfactory quality and quantity to the military and civilian employees of the Department of Defense.

CURRENT SECTION 501 OF THE DOD APPROPRIATIONS
AUTHORIZATION ACT - CIVILIAN PERSONNEL
P.L. 93-365

Section 501. (a) (1) For the fiscal year beginning July 1, 1974, and ending June 30, 1975, the Department of Defense is authorized an end strength for civilian personnel as follows:

- (A) The Department of the Army, 358,717;
- (B) The Department of the Navy, including the Marine Corps, 323,529;
- (C) The Department of the Air Force, 269,709;
- (D) Activities and agencies of the Department of Defense (other than the military departments), 75,372.

(2) The end strength for civilian personnel prescribed in paragraph (1) of this subsection for the fiscal year ending June 30, 1975, shall be reduced by 32,327. Such reduction shall be apportioned among the Army, Navy, Air Force, and activities and agencies of the Department of Defense as the Secretary of Defense shall prescribe. The Secretary of Defense shall report to Congress within 60 days after the date of enactment of this Act on the manner in which this reduction is to be apportioned among the military services and the activities and agencies of the Department of Defense and among the mission categories described in the Manpower Requirements Report. This report shall include the rationale for each reduction.

(b) In computing the authorized end strength for civilian personnel there shall be included all direct-hire civilian personnel employed to perform military functions administered by the Department of Defense (other than those performed by the National Security Agency) whether in permanent or temporary positions and whether employed on a full-time, part-time, or intermittent basis, but excluding special employment categories for students and disadvantaged youth such as the stay-in-school campaign, the temporary summer aid program and the Federal junior fellowship program and personnel participating in the worker-trainee opportunity program. Whenever a function, power, or duty or activity is transferred or assigned to a department or agency of the Department of Defense from a department or agency outside of the Department of Defense or from a department or agency within the Department of Defense, the civilian personnel end strength authorized for such departments or agencies of the Department of Defense affected shall be adjusted to reflect any increases or decreases in civilian personnel required as a result of such transfer or assignment.

(c) When the Secretary of Defense determines that such action is necessary in the national interest, he may authorize the employment of civilian personnel in excess of the number authorized by subsection (a)

of this section, but such additional number may not exceed one half of one per centum of the total number of civilian personnel authorized for the Department of Defense by subsection (a) of this section. The Secretary of Defense shall promptly notify the Congress of any authorization to increase civilian personnel strength under the authority of this subsection.

APPROPRIATED FUNDS CANNOT SUPPORT EXCHANGES
10 USC 4779 (ARMY) & 9779 (AIR FORCE)

Section 4779. Use of public property

(a) When the economy of the Army so requires, the Secretary of the Army shall establish military headquarters in places where suitable buildings are owned by the United States.

(b) The Secretary shall assign suitable space for postal purposes at each military post where there is a post office.

(c) No money appropriated for the support of the Army may be spent for post gardens or Army exchanges. However, this does not prevent Army exchanges from using public buildings or public transportation that, in the opinion of the office or officer designated by the Secretary, are not needed for other purposes.

Section 9779. Use of public property

(a) When the economy of the Air Force so requires, the Secretary of the Air Force shall establish military headquarters in places where suitable buildings are owned by the United States.

(b) The Secretary shall assign suitable space for postal purposes at each air base where there is a post office.

(c) No money appropriated for the support of the Air Force may be spent for base gardens or Air Force exchanges. However, this does not prevent Air Force exchanges from using public buildings or public transportation that, in the opinion of the Secretary, are not needed for other purposes.

STOCK FUNDS
10 USC 2208

Section 2208. Working-capital funds

(a) To control and account more effectively for the cost of programs and work performed in the Department of Defense, the Secretary of Defense may require the establishment of working-capital funds in the Department of Defense to--

(1) finance inventories of such supplies as he may designate; and

(2) provide working capital for such industrial-type activities, and such commercial-type activities that provide common services within or among departments and agencies of the Department of Defense, as he may designate.

(b) Upon the request of the Secretary of Defense, the Secretary of the Treasury shall establish working-capital funds established under this section on the books of the Department of the Treasury.

(c) Working-capital funds shall be charged, when appropriate, with the cost of--

(1) supplies that are procured or otherwise acquired, manufactured, repaired, issued, or used; and

(2) services or work performed; including applicable administrative expenses, and be reimbursed from available appropriations or otherwise credited for those costs, including applicable administrative expenses and costs of using equipment.

(d) The Secretary of Defense may provide capital for working-capital funds by capitalizing inventories. If this method does not, in the determination of the Secretary of Defense, provide adequate amounts of working capital, such amounts as may be necessary may be appropriated for that purpose.

(e) Subject to the authority and direction of the Secretary of Defense, the Secretary of each military department shall allocate responsibility for its functions, powers, and duties to accomplish the most economical and efficient organization and operation of the activities, and the most economical and efficient use of the inventories for which working-capital funds are authorized by this section.

(f) The requisitioning agency may not incur a cost for supplies drawn from inventories, or services or work performed by industrial-type or commercial-type activities for which working-capital funds may be established under this section, that is more than the amount of appropriations or other funds available for those purposes.

(g) The appraised value of supplies returned to working-capital funds by a department, activity, or agency may be charged to that fund. The proceeds thereof shall be credited to current applicable appropriations and are available for expenditure for the same purposes that those appropriations are so available. Credits may not be made to appropriations under this subsection as the result of capitalization of inventories under subsection (d).

(h) The Secretary of Defense shall prescribe regulations governing the operation of activities and use of inventories authorized by this section. The regulations may, if the needs of the Department of Defense require it and it is otherwise authorized by law, authorize supplies to be sold to, or services to be rendered or work performed for, persons outside the Department of Defense. Working-capital funds shall be reimbursed for supplies so sold, services so rendered, or work so performed by charges to applicable appropriations or payments received in cash.

(i) Reports annually shall be made to the President and to Congress on the condition and operation of working-capital funds established under this section.

DOD REORGANIZATION AUTHORITY
10 USC 125

Section 125. Functions, powers, and duties: transfer, reassignment, consolidation, or abolition.

(a) Subject to section 401 of title 50, the Secretary of Defense shall take appropriate action (including the transfer, reassignment, consolidation, or abolition of any function, power, or duty) to provide more effective, efficient, and economical administration and operation, and to eliminate duplication, in the Department of Defense. However, except as provided by subsections (b) and (c), a function, power, or duty vested in the Department of Defense, or an officer, official, or agency thereof, by law may not be substantially transferred, reassigned, consolidated, or abolished unless the Secretary reports the details of the proposed transfer, reassignment, consolidation, or abolition to the Committees on Armed Services of the Senate and House of Representatives. The transfer, reassignment, consolidation, or abolition concerned takes effect on the first day after the expiration of the first 30 days that Congress is in continuous session after the Secretary so reports, unless either of those Committees, within that period, reports a resolution recommending that the proposed transfer, reassignment, consolidation, or abolition be rejected by the Senate or the House of Representatives, as the case may be, because it--

(1) proposes to transfer, reassign, consolidate, or abolish a major combatant function, power, or duty assigned to the Army, Navy, Air Force, or Marine Corps by section 3062(b), 5012, 5013, or 8062(c) of this title; and

(2) would, in its judgment, tend to impair the defense of the United States.

If either of those Committees, within that period, reports such a resolution and it is not adopted by the Senate or the House of Representatives, as the case may be, within the first 40 days that Congress is in continuous session after that resolution is so reported, the transfer, reassignment, consolidation, or abolition concerned takes effect on the first day after the expiration of that forty-day period. For the purposes of this subsection, a session may be considered as not continuous only if broken by an adjournment of Congress sine die. However, in computing the period that Congress is in continuous session, days that the Senate or the House of Representatives is not in session because of an adjournment of more than three days to a day certain are not counted.

(b) Notwithstanding subsection (a), if the President determines it to be necessary because of hostilities or an imminent threat of hostilities, any function, power, or duty, including one assigned to the Army, Navy, Air Force, or Marine Corps by section 3052(b), 5012, 5013, or 8062(c) of this title, may be transferred, reassigned, or consolidated. The transfer, reassignment, or consolidation remains in effect until the President determines that hostilities have terminated or that there is no longer an imminent threat of hostilities, as the case may be.

(c) Notwithstanding subsection (a), the Secretary of Defense may assign or reassign the development and operational use of new weapons or weapons systems to one or more of the military departments or one or more of the armed forces. However, notwithstanding any other provision of this title or any other law, the Secretary of Defense shall not direct or approve a plan to initiate or effect a substantial reduction or elimination of a major weapons system until the Secretary of Defense has reported all the pertinent details of the proposed action to the Congress of the United States while the Congress is in session.

(d) In subsection (a) (1), "major combatant function, power, or duty" does not include a supply or service activity common to more than one military department. The Secretary of Defense shall, whenever he determines it will be more effective, economical, or efficient, provide for the performance of such an activity by one agency or such other organizations as he considers appropriate.

STATE SALES OR USE TAX IN FEDERAL AREAS
4 USC 105

Section 105. State, and so forth, taxation affecting federal areas; sales or use tax

(a) No person shall be relieved from liability for payment of, collection of, or accounting for any sales or use tax levied by any State, or by any duly constituted taxing authority therein, having jurisdiction to levy such a tax, on the ground that the sale or use, with respect to which such tax is levied, occurred in whole or in part within a Federal area; and such State or taxing authority shall have full jurisdiction and power to levy and collect any such tax in any Federal area within such State to the same extent and with the same effect as though such area was not a Federal area.

(b) The provisions of subsection (a) shall be applicable only with respect to sales or purchases made, receipts from sales received, or storage or use occurring, after December 31, 1940.

CHAPTER 12

CONCLUSIONS AND RECOMMENDATIONS

12-1. CONCLUSIONS.

a. General.

(1) Implementation of PBD 282 suggests abrupt and sweeping reorganization to achieve the economies necessary to sustain the systems. However, cautious, sensible planning is necessary to prevent actions from outstripping the capability of management and available systems to execute changes. The study group, recognizing limitations of current organizational structures within the services, has, therefore, concluded that a conservative approach to structural changes is essential at this time. This conclusion was reinforced by both the cost analyses of the different alternatives and evaluation of the current status of the commissary systems of each of the services. The overriding requirement upon which actions must be based is the attainment of the maximum possible monetary savings for patrons within the time constraints of the budget proposal. The extent to which this requirement is met will determine the long-term success of the commissary system as a valuable benefit.

(2) There are a number of urgent requirements recognized by the study group for the development and implementation of major system, policy, procedural and other changes in order to retain the commissary system as a valuable benefit. These requirements for change exist at Congressional and Office of the Secretary of Defense levels and within each of the military services. They also exist regardless of organizational alternatives selected.

(a) Customer education and information programs are necessary because various surveys reveal that commissary customers perceive current savings to be less than they actually are under even the lowest savings estimates. Depending on the survey, customer perceptions vary widely. For example, one survey depicts that customers perceive only a 7 percent savings while another reveals customers perceive savings of 18 percent, both of which are less than the 22 percent actual savings estimated by the study group. Customer perceptions are the key to the amounts of sales losses that will occur as commissary prices increase to levels approaching supermarket prices.

(b) Price comparison on the part of customers, previously of minor importance, assumes a major

role in the future. The study group is of the opinion that significant savings can be retained if the majority of customers accurately perceive such savings and continue to shop in commissaries. However, should this not occur, sales losses could be dramatic and be of sufficient magnitude to threaten the viability of commissaries.

(c) Examination of commercial practices reveals that items are sold at widely varying percentages above and below product cost. Knowledgeable sources have advised that as many as 600 to 700 items are continually sold below cost in commercial supermarkets. Gross margins for other items range from 1 percent to about 35 percent. An estimate provided to the study group is that if a single markup were added to each item sold in the commissary, more than one-fourth of the commissary items would be priced higher than like items in commercial supermarkets. These items would consist largely of the more essential basic food items which have lower markups in comparison to convenience and higher food budget type items. Such a system would impose a relatively greater proportion of operating costs on lower income families in addition to reducing commissary sales volumes. For these reasons, variable pricing of commissary items is essential and should be implemented not later than 1 October 1976, so as to preclude the losses of large numbers of customers.

(d) Variable pricing requires that those services currently accounting for items at cost price revise their accounting and associated procedures so as to account for items at selling prices, i.e., adopt a retail accounting system. Only by this method can the accuracy and integrity of the commissary accounts be maintained.

(e) The magnitude of the changes required to organizational structures, management information, data processing, accounting and other systems is such as to require exceptional actions to accomplish the essential changes by 1 October 1976. Determination and commitment on a full-time basis of sufficient personnel with the requisite specialties to meet prescribed time frames are indispensable to orderly and successful implementation regardless of the alternative finally approved. Shortening of time frames normal for development of changes of these types is required.

(3) The study group has utilized estimates of sales losses throughout its deliberations; however, these losses cannot be forecast with the precision necessary for

exact planning. It is also appreciated that expenses within the commissary system are relatively fixed over short periods of time. The committee has, therefore, made its recommendations under the dual assumptions that: strong customer information programs will be developed to inform commissary customers of their savings levels, and that additional flexibility will be permitted the commissary systems to assist in controlling costs, particularly with regard to personnel utilization and pricing.

b. Factors Bearing on Selection of Alternatives.

Determination of the most efficient and economical management structure and method of operation for commissary stores is a complex undertaking for the reasons listed below:

(1) Major differences exist between the management structures and methods of operation of the various services' commissary programs which make attempts at accurate comparison and cost analyses exceedingly difficult. These differences exist not only in data collection and processing systems but also in the areas of accounting, procurement, inventory control and even in terminology to a degree which makes it almost impossible to isolate costs associated with commissary stores in order to make meaningful comparisons.

(2) Alternative funding methods (either appropriated or non-appropriated) having differing rules and regulations concerning their use impact differently on personnel and operating costs.

(3) The interdependence of the commissary store system and the Defense Personnel Support Center (which procures, warehouses and transports troop issue and commissary resale merchandise) impacts on structural alternatives. Both the troop issue and resale functions benefit from this relationship. For example, the resale commissary systems benefit by avoiding duplicative procurement and distribution costs. Similarly, Defense Personnel Support Center is able to economize on certain appropriated fund costs for troop issue such as reduced transportation costs through being able to make carload shipments of combined resale and troop issue subsistence.

(4) The indirect support that commissary stores receive for various functions has become entwined in the

fabric of other organizations and is impossible to identify with any degree of precision.

(5) The necessity of developing new organizational structures and methods of operation for commissary stores at the same time that they are becoming self-supporting for direct labor costs introduces many uncertainties. These include the extent to which price increases will reduce commissary sales and discretionary disposable income and the effect this will have on exchange sales, the welfare and recreation programs they support and other non-appropriated fund organizations.

(6) Differences between overseas and CONUS commissary operations and the necessity that commissary support be provided at remote locations (both within and outside the US) regardless of overhead costs restrict efforts to achieve optimum efficiency and effect standard structural and operational realignments.

(7) The Navy's utilization of commissary stores for sea/shore rotation of enlisted personnel impacts on the problem because costs and service are affected by rotation and recurring training requirements.

(8) The magnitude of the commissary store program, geographical dispersion of the stores throughout the United States and overseas and variances in store sizes from very small stores to "super" stores, doing in excess of \$2 million in sales per month, introduces variables that make a single answer to the question of what is the most efficient and economical management structure and method of operation extremely difficult to determine. Examples of the variables include:

(a) Methods of distribution applicable to CONUS require extensive modifications for overseas shipments.

(b) Centralized distribution systems, at best, would be limited to specified areas due to low commissary densities in most areas.

(c) Unavoidably high overhead costs exist at certain locations as outlined in the preceding paragraph.

c. Potential Areas for Improvement of Existing Systems.

(1) Chapter 5, Volume 1 and its corresponding appendices in Volume 2 include potential areas of improvement which the study group has identified. These include the areas

of data systems, functional consolidations, facilities improvements, personnel utilization, personnel training, and operations.

(2) Analysis of commercial standard chain store operations, coupled with independent industry advice and separate analysis of commissary operations, reveal a need to achieve manpower economies through increased utilization of other than full-time employees for peak workload requirements. Only the Navy has progressed in this area, thus, there is a need for increased emphasis.

(3) Functional consolidations are separately discussed in the next section. However, there are two other major areas requiring appropriate emphasis.

(a) An urgent need exists for development and implementation, at the earliest possible date, of an effective automated management and information system(s) to provide for effective management under either central management alternative (separate service or joint service). Although one standard system would appear desirable, the delay required to achieve such a system is unacceptable for the reasons previously discussed and since it would be costly both to patrons and appropriated funds. Coordination between the services to achieve systems as nearly identical as possible without delaying implementation would promote eventual standardization at such time as it could be implemented.

(b) Commissary operational efficiency is adversely impacted by outmoded facilities, including isolated warehouses, which increase operating costs and impair customer service. Once sales losses have been determined and sales volumes have stabilized, there is a need for accelerated construction programs within each service to overcome this problem .

d. Required Changes to Current Legislation.

A self-supporting commissary system requires and justifies four changes to existing legislation. It requires these changes since present law unnecessarily increases cost to the detriment of the patron and detracts from the efficient operation of the system. It justifies these changes since all of the current laws were enacted in contemplation of a commissary system using appropriated funds for direct cost. These changes are:

(1) Variable Pricing:

The Army and Air Force are now required by law to sell each commissary item at invoice cost. The

requirement to reimburse certain costs contained in annual Appropriation Acts, has been accomplished by a level surcharge collected at the register, thus, preserving the shelf price at invoice cost. This requirement, to sell each item at cost, must be changed to allow variable pricing as previously discussed.

(2) Invest customer generated funds.

Business with substantial cash flow invariably receives income from investment of such funds. The Army and Air Force Exchange Service realized over \$4 million income from investments in their last fiscal year. Surcharge, collected from the customer, will increase dramatically as commissaries increase markups to accumulate construction funds and to pay labor cost. Investment of these funds, in short and long term obligations, would be a substantial boost to the economic viability of a more self-supporting commissary system. The safety of the funds could be assured by statutory authority limiting investments to US obligation.

(3) Remove Distance, Price and Adequacy Criteria from the Appropriation Act.

The Secretary of Defense must now certify that items normally procured from commissary stores are not available within a reasonable distance, at a reasonable price or in reasonable quality and quantity, before annual appropriations may be used to operate commissaries. This provision will have lost its reason for being when these operations are directly supported by customer generated surcharge. To continue this requirement would assess the commissary customer for expenses that do not contribute to efficient operations.

(4) Remove manpower end-strength restrictions on commissaries.

Since the customer will be supporting labor cost for civilian employees, end-strength restrictions will not serve to limit cost to appropriations. These restrictions unduly inhibit effective management of the commissary labor force. The law now requires ceilings to apply equally to permanent or temporary, full-time, part-time, or intermittent employees. This forces commissaries to use an excess of more costly full-time personnel to stay within ceilings when use of other than full-time employees would reduce cost. It also involves the commissaries in command imposed hiring freezes, etc. which cause significant manning deficiencies during peak sales periods.

e. Management/Structural Alternatives.

(1) All alternatives examined are possible except contractor operations. This conclusion presumes that the number and locations at which stores are operated would remain essentially unchanged. Any action which would substantially reduce total sales would adversely influence this conclusion.

(2) Economies obtainable under the central management alternatives appear to be sufficient to permit reimbursement for direct costs as proposed, retain significant savings for customers and maintain a workable commissary system.

(3) The time constraint imposed for the commissary system to achieve the capability to reimburse for 100 percent of personnel and oversea utility costs, severely inhibits the orderly implementation of each alternative.

(4) Separation of the wholesale procurement and distribution mission for commissary stores from the Defense Personnel Support Center (DPSC) as suggested under Alternative 2 (Merger with the Exchange System) could increase the appropriated fund costs of that activity for troop issue. It would also reduce the capability of the DPSC to perform its mission during mobilization because of reductions in staffing and would place elements of DOD in competition with each other in the market place.

(5) Responsibility for troop issue is a command function. Under the self-sustaining concept, precise identification of costs properly charged to both the troop issue and commissary store functions is essential. The study group recognizes that the Army and Air Force have recently modified their reporting and budgeting systems to further the concept of separating costs. It is also realized that identification of such costs could best be achieved through complete physical separation of these functions which might not be cost effective in every instance. It is concluded that the services concerned should develop procedures which will ensure equitable reimbursement for support provided by one entity (commissary store or troop issue) for the other.

(6) Alternative 1 (Centralized Management Within Each Service) has the least impact on both patrons and commissary personnel of all alternatives examined. Each service has the capability to achieve centralized management within the time frame imposed with the least disruption to the system,

while retaining both savings and customer service at adequate levels. Also, this alternative keeps the services' options open until the full impact of PBD 282 is felt and customer reactions can be determined with certainty. If adopted, Alternative 1 would require priority actions to develop and implement necessary control mechanisms and requisite management and information systems as previously outlined.

(7) Alternative 2 (Merger with the Exchange Systems). Depending upon the method of allocating overhead costs and other income, could provide marginally lower savings to the patron than those obtainable under Alternatives 1 and 3. The Army and Air Force Exchange Service has an automated data processing system which, with appropriate modification, could support commissary requirements. This alternative would provide flexibility in management of personnel, provide a wide base for career progression and produce system efficiencies as a result of the merger. This alternative could result in major personnel turbulence at the time of merger plus a substantial loss of existing managerial/supervisory personnel. Moreover, possible transfer of procurement support from DPSC to the exchange services would adversely impact the total DPSC mission. For these reasons the exchange alternative is less desirable at this time than central management within the services.

(8) Alternative 3 (Joint Service Commissary Agency). The cost analysis of all alternatives contained in Appendix 11, Volume II, indicates this alternative provides the greatest overall cost reductions and customer savings. It would also require a minimum lead time of 3 to 5 years. A major deterrent to immediate implementation is the lack of an existing automated management and information system. This alternative is, therefore, not obtainable within the time frame imposed by Program Budget Decision 282. The uncertainties of future sales, savings, and the allocation and assessment of costs also suggest prudence. Therefore, it seems inappropriate to recommend an alternative that cannot be implemented for several years.

(9) Alternative 4 (Government Owned Contractor Operated) results in significantly lower savings than any other alternative and is, therefore, impracticable.

12-2. RECOMMENDATIONS.

a. Each military service should adopt centralized management of its commissary stores.

b. Concurrently, the military services should develop necessary commissary accounting and ADP systems. The early

establishment of a joint-service committee may be desirable to promote standardization to the extent feasible.

c. Enabling legislation be enacted to:

(1) Delete the requirement that Army and Air Force commissary stores sell each item at invoice cost to permit variable pricing.

(2) Permit funds generated from adjustments of or surcharge on selling prices in commissary stores to be invested.

(3) Delete the last sentence of Section 814 of the Defense Appropriations Act which establishes availability, distance and price criteria for certification of commissary stores.

(4) Add a clause to paragraph 501b of the Defense Appropriations Act excluding commissary employees from end-strength restrictions on civilian personnel to provide flexibility in use of other than full-time employees.

d. The Civil Service Commission be requested by the Department of Defense to provide special recruiting support for employment of a greater number of other than full-time employees.

e. The services should develop programs to communicate relevant commissary operating and savings information to authorized customers.

f. The resale and troop issue functions should be separated and all support provided by one entity (resale or troop issue) for the other be on a fully reimbursable basis.

g. Effective training programs should be developed to enhance job efficiency in the various commissary functional areas.

h. After the services have separately adopted centralized management and have been operational for a sufficient period of time to evaluate customer losses and operational costs, the services should assess whether consolidation into a joint-service commissary system would be cost advantageous to the customers. Such assessment should also focus on the desirability of lesser consolidation such as an Army/Air Force commissary system.

CHAPTER 13

SUMMARY OF SERVICE COMMENTS AND RECOMMENDATIONS

13-1. GENERAL. It is the purpose of this chapter to summarize the major comments and recommendations received from each of the individual services concerning the Draft Study of Military Commissary Stores. Considerations and responses by the study group to these major recommendations are also provided in this chapter. The detailed comments and recommendations from each of the services and the study group's responses are contained in Appendices 13-A through 13-C, Volume II.

13-2. ARMY.

a. The Department of the Army reply expressed concurrence with the draft study. The major comment pertained to the urgent requirement for development of an automated system for central management of commissary stores.

b. The study group fully recognizes the vital part that an effective automated system must play in the comprehensive management and information system which is essential under centralized management. In order to achieve the maximum potential savings in both direct and indirect costs and to assure maximum savings to commissary store customers, priority emphasis must be directed toward the development and implementation of a management and information system for Army commissary store operations. Paragraph 6-A.7., Appendix 6-A, Volume II of the study, addresses the estimated cost impact which delayed implementation of a management and information system will have under a central management concept.

13-3. NAVY.

a. The Department of the Navy reply recommended that the Navy commissary stores merge with the Navy exchanges and that the Marine Corps commissary stores and exchanges retain their current organizational structure.

b. The study group concurs with the intention of the Department of the Navy to continue refining the organizational structure and management techniques of Navy commissary stores and exchanges. The analyses made indicated that a Joint Service Commissary Store System appeared to provide the most customer savings while having the least impact on customers and personnel. However, the first steps toward

the Joint Service Commissary Store System must be the verticalization of command and control of Army and Air Force Commissary Store Systems and the development of effective automated data systems. After all services have been operational in a centralized mode for a sufficient period of time, the completion of the final recommendation, the assessment of consolidation into a Joint Service Commissary Store System, may indicate that this type of system would not be cost advantageous to customers and/or that another alternative would be more desirable.

c. The study group concurs that the Marine Corps should evaluate the feasibility of consolidating where economies can be achieved with emphasis given to administration, procurement, inventory control, and accounting. Moreover, we believe they should consider implementation of those other areas identified as potential improvements for the existing system (Chapter 5).

13-4. AIR FORCE.

a. The Department of the Air Force reply essentially concurred with the recommendations of the report.

b. It highlighted the need to develop commissary accounting and ADP systems on an expedited basis to enhance efficiencies of a centralized management system.

c. It also requested the latitude to contract individual commissary stores on a test basis within the framework of a centralized Air Force Commissary System. In this regard, the study group sought and received the benefit of the most extensive, detailed information and discussions ever provided by the retail grocery industry. These in-depth consultations indicated that there were no formulas available under existing statutes and industry conditions by which commissary operations could be contracted out and still retain the necessary level of customer savings. It is therefore recommended that any test of contract commissary operations include adequate provision for restoration if the test proves unsuccessful.

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