

**STATEMENT OF
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Mr. Chairman and Members of the subcommittee, it is my pleasure to appear before you to provide the Defense Commissary Agency's (DeCA) update for this past year. It was a year filled with successes as once again DeCA received positive results in sales growth and customer service. It was also a year of challenges as we prepared for BRAC and re-stationing initiatives; continued our reorganization and centralization of Agency support functions; re-engineered processes to increase the value of the benefit without increasing its cost; and confronted rising construction costs. Finally, it was a year of heartaches as we picked up the pieces and rebuilt stores damaged or destroyed by the devastating forces of nature that struck the Gulf Coast. Reflecting upon how these successes were achieved, the challenges met, and the heartaches faced made me recognize that never in my 40 years in the grocery business have I been prouder to be associated with a group like the 18,000 employees who operate the commissary system and do such a great job running our 268 stores worldwide. Through them, again this year DeCA demonstrated, with astonishing business results and facing significant resource challenges, why it remains at the heart of the Quality of Life benefit for the men and women of our great nation who proudly wear or wore the uniform of our Armed Services.

Fiscal year 2005 was another impressive year for DeCA. Once again the numbers really said it all—sales were up, costs were down, customer satisfaction measurements increased even higher and customer savings remained constant. You may recall that last year we were pleased that our sales increased 3.9 percent, or \$197 million. This year they went up an additional 2.5 percent, or another \$133 million, for total annual sales of \$5.36 billion. Meanwhile, the commercial supermarket sector again continued to lag. At that same time our costs came in under program. In fact, when measured in constant Fiscal Year 2000 dollars, the administration of the commissary benefit today remains below what it cost in 2000. This reduction in constant

dollar cost has been gained—not at the expense of our customers—but because of the efficiencies we developed and deployed throughout the Agency. As our overall customer service score, of 4.55 on a scale of 5, demonstrates—the patrons like what we do. These internal measurements were validated externally by the American Customer Satisfaction Index (ACSI), which this year raised DeCA’s FY 2005 score to 77. The score of 77 remains three points higher, a statistically significant difference, over the national average score for commercial supermarkets. Of course, customer savings remain the core of the commissary benefit. It is the level of savings that we provide to the military community and the fact that we deliver the same level of savings to all locations including remote locations and overseas environments that make the commissary benefit one of the highest valued benefits provided our military personnel. Of course, we would not be able to achieve this level of savings for our military families without the tremendous support our trading partners provide in pricing and promotion of their products. I would like to take this opportunity to publicly acknowledge and thank them for their support of the commissary benefit.

We compare over 30,000 identical meat, produce, and grocery items to compute the overall average savings. This item to item comparison, weighted by volume, is the only valid method to truly report savings. We also took into consideration the fact the leading grocer no longer reports pricing information. We applied a 2.42 percent reduction on our savings to take into consideration the “Wal-Mart effect.” Even after assessing that reduction, patron savings for commissary sales remains at 32 percent. Performance results like these make it possible for us to set a self imposed goal of *increasing the value of the benefit without increasing costs*.

While the statistics, like those above, are a common means of viewing the performance of a retailer, DeCA has also demonstrated it possesses the governance attributes of a model

governmental entity. Being fiscally responsible continues to be one of DeCA's priorities and I am extremely pleased to report for the fourth consecutive year DeCA has received a clean audit opinion on its financial records. That audit not only looks at all of our money accounts—sales, surcharge, capital investment and the operating funds annually appropriated, but also daily activities such as how accurately we record time and attendance and maintain physical inventory and accountability of assets, whether in the stores or at headquarters. Our successes have been noted by others, particularly the DoD Comptroller who has designated DeCA as a “poster child” for financial reporting excellence.

We have also been recognized as a leader in the implementation of OMB Circular A-123 and our aggressive approach to meeting financial reporting requirements has been cited by DoD as a model for attaining A-123 compliance. Tied to financial reporting, the A-123 process imposes strict requirements on the internal controls an agency uses to make, and keep, it fiscally sound. In large part, A-123 is a tool to help agencies achieve a clean audit opinion by requiring a review of a maximum of eight of its financial processes each year. The bar is higher for agencies, like DeCA, who have received a series of unqualified opinions. They have to review every process, in our case a total of 19, to ensure we can identify and address any weakness that could jeopardize the receipt of unqualified opinions in the future.

The number of installation closures under BRAC 2005 that will affect commissaries was not as great as anticipated. Only seven installations with a commissary store are scheduled to close. However, the resulting realignments due to closures and announced realignments will significantly affect the delivery of the commissary benefit. In many locations our stores will be too small, which creates greater challenges as we evaluate increased capacity requirements and

available funding alternatives. The completion of this task has been made more complex because the overseas global re-stationing requirements have not been finalized.

While DeCA's reorganization plans were on the verge of being implemented prior to the BRAC Commission's findings, several of our activities that occupy leased facilities will be relocated to the Agency headquarters building at Fort Lee as a result of BRAC 2005. We anticipate that the leased facilities occupied by our region headquarters at Virginia Beach and the former region in San Antonio will be closed and the remaining personnel relocated by the end of this year. The personnel in our Hopewell, Virginia leased facility cannot be relocated until the construction of an addition to the headquarters building is completed. BRAC 2005 also transferred our personnel servicing office, currently located in Arlington, to the Defense Logistics Agency with operations to be performed in Columbus, Ohio. That move will not be made until after DeCA's conversion to the National Security Personnel System.

At the heart of our reengineering efforts is the establishment of goals to best deliver the commissary benefit in a manner that balances the best interest of the patron and the taxpayer. Its purpose is to drive unnecessary costs out of the system so that we can reinvest those dollars to increase the value of the commissary benefit for the patron. To that end we have focused our reengineering efforts to optimize our business processes using Lean Six Sigma. We have recently completed the first phase of six projects. Examples of processes examined include equipment inventory accountability and replacement, standardizing commercial activity contracts, and revising receiving procedures to better adopt commercial practices to account for shortages and breakage.

Perhaps one of our larger challenges is increased construction costs. Over the last two years many of our projects have been impacted by the increased cost of building materials

(notably concrete and steel), fuel, and utilities. In some cases we have had to defer planned projects in order to have sufficient funds to pay for others, or reduce the size of projects coming in at a cost that was more than expected. These general economic increases have been exacerbated by the heavier demands, and further increases in cost, for building materials because of the devastation caused by Hurricanes Katrina and Rita. Further, the requirement to incorporate force protection and antiterrorism standards in our construction designs has also negatively impacted the surcharge account. While the Surcharge Revitalization Plan you enacted in 2000 realigned funds to mitigate the shortage in capital investment dollars, that Plan was not designed to accommodate the huge increases due to today's shortage of the construction materials. Without your foresight in 2000 we would probably have had only enough surcharge to perform required repair and maintenance on our stores.

Like many other Americans, military families too suffered from the devastation this seasons natural disasters inflicted upon the Gulf Coast. A number of DeCA facilities were affected by those hurricanes. The damage and destruction caused by Hurricane Katrina was particularly demoralizing. When the winds died away our Gulfport store was unusable and the Keesler store was under five feet of water, and subsequently had to be demolished. The New Orleans store fared better, suffering primarily product loss. With the assistance of the military Services we were able to set up temporary facilities to provide the basic required needs for military families as they returned to those installations. The speed with which the damage was assessed, alternate facilities identified and adapted for use, equipment delivered and shelves stocked was astounding, particularly when you recall the logistic nightmares wreaked by Hurricanes Katrina and Rita on the transportation networks in the southern area of our country. Our people who worked tirelessly and often around the clock making those temporary facilities

operational told me they received the best reward possible—the smiles on the faces of those thankful patrons as they returned to shop in their commissaries. The commissary at New Orleans reopened September 29th and the repairs at Gulfport are scheduled to be completed in May. But we still have a lot to do at Keesler, which requires re-building from the ground up. All of this has been made possible by your efforts, and those of your colleagues to reimburse the losses suffered. On behalf of the men and women who work for DeCA and all the commissary patrons affected by last years storms, I want to thank you for the supplemental funding that made this possible.

As I mentioned last year, senior leaders at DeCA have visited with the senior management at a number of our top trading partners to discuss the most probable future of the grocery industry. These top-to-top visits have enabled DeCA to benchmark against the best practices industry uses and develop a number of underlying initiatives to increase the value of the commissary benefit without increasing its cost. Some of those programs are:

Partnering with TRICARE, DeCA has developed the “It’s Your Choice, Make It Healthy” program to highlight those healthy foods available in military commissaries. This partnership not only informs military families about eating healthier, controlling their weight and promoting concepts such as weight management and fitness, but also "financial fitness" through savings they obtain shopping the commissary. Many of our larger commissaries have already been configured with “Wellness Centers” to highlight these products for health conscious patrons. Further, combined with this initiative is an increased selection of natural and organic foods we are adding to commissary aisles. We view the “It’s Your Choice, Make It Healthy” and the TRICARE partnership as natural extensions of our mission that fit well with the OSD

health and wellness program, because if any group of American's should be healthy, it is the members of our armed forces.

We have entered cyberspace deploying our Internet venture—the Virtual Commissary. Activated in October 2005, it features gift packs of items, at commissary negotiated prices, which may be ordered directly from partnering companies through the mail. Virtual Commissary usage is restricted and shopper eligibility is determined through accessing the Defense Enrollment Eligibility Reporting System (DEERS) database. For the second stage of the Virtual Commissary's deployment, we are seeking a contractor to pick, pack and ship individual products ordered by authorized patrons from a selection of 300 to 500 commissary items, again at commissary prices plus a fee for shipping and handling, for delivery to their location. We are excited about the potential this concept would provide a commissary benefit for our patrons who are not close to a commissary. This should be a particularly valuable extension of the commissary benefit for Guard and Reserve families and those deployed to forward areas.

We are changing the method in which we obtain produce for sale in commissaries. In the past, produce for DeCA's 268 commissaries worldwide was acquired through a cooperative arrangement with the Defense Supply Center – Philadelphia (DSC-P). During the first nine months of 2005, DeCA tested commercial industry practices to provide fresh fruit and vegetables for 20 of our commissaries, serviced by a commercial firm in Tidewater Virginia. The contractor utilized approximately 79 small business concerns, including local farmers, small disadvantaged businesses and veteran owned businesses, providing produce for our stores using the commercial sector model. The results delivered were impressive—

- Produce was cheaper. Patron savings increased 17 percent.
- Produce freshness and quality improved.

- Tonnage sold increased over 25 percent.
- Average order lead-time was reduced by 50 percent.
- The web-based ordering system fielded with this test simplified and streamlined the ordering process.
- Produce managers had more time to spend on the sales floor overseeing the produce operation.
- Produce delivery time and frequency were more consistent with store requirements.
- DeCA labor efficiency improved because the industry support system (i.e., ordering and quality assurance) was more reliable.

Because the DeCA Produce Test results validated the business concept as a more efficient business approach, the Department of Defense decided DeCA should assume responsibility for contracting for its resale fresh fruit and vegetables.

Maintaining a 100% set-aside commitment for small business participation, the produce supply contracts will be competitively awarded. Based upon produce industry inputs, the United States has been divided into geographic areas for contracting purposes. The first competitively awarded contract for 22 stores in the mid-Atlantic area was completed in September 2005. The next area to be converted will be the Midwest section of the United States. The solicitation covering that area was issued last month. Additional solicitations will follow for the other areas at approximately six-week intervals. By September 30, 2006, DeCA will have its contractors supplying all commissaries worldwide. Adoption of this proven commercial approach to produce acquisition supports DeCA's goal to improve its efficiency and effectiveness in the provision of the commissary benefit. Further, directly outsourcing produce results in lower costs to DeCA, the government, produce suppliers, and the patron.

In early 2004, we developed a prototype store concept designing a store workforce that was simple, easy to manage, cost effective, more productive and maximized the changes anticipated by implementation of the National Security Personnel System. The final workforce model eliminated 12 different position descriptions, replacing them with two—a multi-skilled Store Associate and a General Manager. To ensure that employees can be assigned various duties to meet mission requirements, a 2-year training plan was developed to teach employees how to perform all store functions. The training plan teaches them the fundamentals of the grocery business, allows them to determine the area in the store where they have the greatest interest and skill, and prepares them to move upward into management. Our first two prototype stores—Smokey Point, Washington and Grand Forks Air Force Base, North Dakota—have demonstrated the success of this concept. We began expanding this workforce concept to other stores last month.

About the same time, DeCA revised the concept it used in conducting A-76 studies. At that time, in order to achieve the efficiencies we needed for the future, to avoid the potential to have multiple contractors in each store and to ensure our employees had a competitive opportunity in these studies, we changed the way we did business. We did two things: (1) created a new “prototype” workforce model, described above, based upon that used in the commercial grocery industry, and (2) ceased performing the study of each separate function—i.e., meat department, grocery department, produce department and cashiers—combining them together in one store-wide study.

While we were above target for our DoD A-76 target goals at the end of Fiscal Year 2005, the legislation enacted last year placed a moratorium on performing A-76 studies in our stores until December 31, 2008, providing an unexpected opportunity to deploy the prototype

workforce without having to simultaneously conduct A-76 studies in our stores. We believe that the time offered by this moratorium will allow us to build a workforce that (1) meets DeCA's need for a more flexible workforce, (2) positions DeCA's employees for a smoother transition to the National Security Personnel System (NSPS), (3) creates the potential that the prototype workforce may be designated as an alternative to conducting future A-76 studies, or (4) positions the government workforce to be more competitive in future A-76 studies should they be required.

On the IT front, we were pleased that procurement of our new front end system, the Commissary Advanced Resale Transaction System (CARTS), came in well below the government estimate. Awarded to IBM, the contract offered a much more technologically advanced system, relying on less hardware and thus a cheaper maintenance tail. Those technological advancements saved commissary patrons \$92 million of their surcharge funds that can now be used to fund other requirements. We are also well under way in development of the DeCA Enterprise Business System (DEBS) that will replace several legacy business applications. DEBS will support business process reengineering efforts, meet industry mandates, improve system interoperability through data standardization and use of business enterprise architecture standards and lower system sustainment costs by reducing their complexity and data redundancy.

We are also proud of the measures we have taken to protect our customers from identity theft. We have integrated the best protection software and hardware that Government and industry have to offer to deploy the most secure encryption system in the military resale enterprise and one of the best in the retail world. Using the latest encryption standards for wireless and the wired components of our infrastructure, our intrusion detection systems and firewalls protect and defend our systems against more than 2000 attempts each month to crack

into our network. We were particularly proud to have earned the second highest score for data protection in DoD for 2005.

Of course, our primary focus always remains on the patron and particularly on reaching those who are not taking advantage of their commissary privilege. We use a number of vehicles to reach out to these individuals. A group of industry members has formed a Consumer Awareness Team that has provided books of coupons redeemable only in the commissary to attract newcomers. Both NEXCOM and AAFES have been particularly generous in including commissary messages in their mailings to their customers. We continue to provide the value of the commissary benefit message at the Service's basic training installations. Commissaries actively participate in all pre-deployment briefs and at family support briefings aimed at Guard and Reserve families. We are continuing to partner with manufacturers and distributors to offer truckload sales of authorized commissary products at Guard and Reserve Centers.

Likewise, we continue to assist our fellow retail organizations as they bring a bit of home to deployed forces in the Mideast. In Fiscal Year 2005, we shipped over \$6 million in product to AAFES and NEXCOM from our distribution center in Europe to support military members in those areas of operation.

The Gift of Groceries continues to be a very popular program to support our military families, particularly in the aftermath of Hurricane Katrina. Since the program began in the fall of 2002, over \$10.5 million in commissary gift certificates have been provided to military families. The public can donate gift certificates to worldwide organizations that assist military families such as the USO, Air Force Aid Society, the Fisher House Foundation and Operation Homefront.

I have been pleased to have the opportunity to tell you about the great things DeCA has accomplished this past year and of its contributions to the quality of life of our military families. When forces deploy, the families left behind depend upon their local community services, including the commissaries, to see them through tough, nervous, lonely times. We, at DeCA, are proud of the contribution we make in operating the 268 commissaries worldwide that provide tremendous savings on groceries for military personnel, retirees and their families. We recognize that commissaries deliver a highly valued component of military compensation in areas where the cost of living is high, and they bring a morale-building “taste of home” feeling by providing familiar American food products in overseas locations where such products are often unavailable. A core military family support element, and a valued element of military pay and benefits, commissaries contribute to total family readiness and enhance the quality of life for America’s military and their families. Next October DeCA turns 15, and we at the Defense Commissary Agency are proud of the role we play in helping recruit and retain the best and brightest men and women to serve our country. Thank you for the continued emphasis you place on the value of the commissary benefit.

I will be happy to answer any questions you may have.