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STATEMENT OF

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H. L. KRIEGER, DIRECTOR
FEDERAL PERSONNEL AND COMPENSATION DIVISION

BEFORE THE

NONAPPROPRIATED FUND PANEL
INVESTIGATIONS SUBCOMMITTEE
COMMITTEE ON ARMED SERVICES
UNITED STATES HOUSE OF REPRESENTATIVES

HSR00501

ON

[THE OPERATION OF MILITARY CLUBS
AND ALCOHOL PACKAGE STORES]

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Mr. Chairman and Members of the Panel:

We appreciate the opportunity to discuss our report "Changes Needed In Operating Military Clubs and Alcohol Package Stores," which was issued to the Chairman on January 15, 1979.

At the Chairman's request, the General Accounting Office made a comprehensive review of the management and operation of the military club system and related alcohol package stores. We examined the club system for the purpose of identifying ways to improve the delivery of needed services in the most efficient, effective, and economical manner. We conducted our review during 1978 at DOD, Army, Navy, Air Force, and Marine Corps' headquarters, at selected major commands, and at 18 military installations in the United States, the Far East, and Europe. As part of our review, we evaluated the operating results for clubs and package stores for fiscal year 1977--the most recent full fiscal period for which data was available.

The military club system and related package stores are an important part of the Morale, Welfare, and Recreation (MWR) Program. MWR activities are essential to the morale and esprit de corps of military personnel and, according to the Department of Defense, contribute to improved combat readiness. The program is intended to provide service members and their families with various types of activities similar to

those available to civilians. The program is also intended to improve individual satisfaction with military life and attract dedicated men and women to military careers. The program is particularly important to military personnel and dependents stationed overseas. It attempts to provide them with a quality of life similar to that enjoyed by their counterparts in the United States.

Within this context, our review showed that certain changes are needed in the operation of the club system. These changes should not be considered as an attempt to reduce or eliminate necessary club services, but as a means of enhancing the quality of such services.

We are convinced that changes are needed because

- military clubs are generally losing money from operations and are dependent on profits from package stores and appropriated fund support for their continued existence,
- military clubs are not effectively meeting the needs of active duty personnel, and
- the present management system of decentralized operational control and centralized policy making has not resulted in needed improvements.

I would like to highlight our report findings in each of these three areas.

FINANCIAL CONDITION OF MILITARY CLUBS AND PACKAGE STORES

Military clubs and alcohol package stores constitute a major business enterprise with gross revenue from sales amounting to \$688 million in fiscal year 1977.

Package store operations generally result in significant profits. During fiscal year 1977, package stores reported net income of \$51 million, most of which was distributed to military clubs and MWR activities.

However, clubs are generally not self-sustaining entities. Although the Services reported net income from operations during fiscal year 1977 totaling \$19 million, 25 percent of all clubs lost money. Without profit distributions from package store operations the clubs would have lost \$16 million, with 57 percent of all clubs reporting losses.

In addition, clubs and package stores received \$93 million in appropriated fund support during fiscal year 1977. This assistance was not reflected in their financial statements but, in effect, reduced the club system's expenditures for a variety of goods and services provided "free." Club income also included \$43 million in membership dues and slot machine profits which were derived from Navy and Marine Corps' clubs overseas.

Without alcohol package store profits, dues, appropriated fund support, and to a lesser extent, slot machine profits, the military club system would be unable to survive and would eventually face bankruptcy unless significant management improvements are made.

Dues or profits from games are normal sources of revenue for operations such as clubs. However, relying on

package store profits has generated considerable disagreement between the Congress and the Military Services. The question of what constitutes a reasonable amount of appropriated fund support is also controversial. Striking an equitable balance between what the taxpayers should fund and what the Service members should pay presents a fundamental problem.

Allocation of package store profits

As early as 1972, the Special Subcommittee of the House Armed Services Committee questioned the prevailing practice of allocating the profits of package liquor sales solely to military clubs. The Subcommittee believed that liquor sales' profits should be provided to the installation welfare fund and be used by the base commander for the benefit of all personnel under his command, not just clubs.

This issue surfaced again during the fall 1977 hearings held by the Nonappropriated Fund Panel and led the Panel to request that GAO analyze the justification and need for distributing alcoholic beverage store profits to clubs.

We reviewed the methods used by each of the Services for distributing package store profits between clubs and other MWR activities. We found that the allocation is generally made by the installation commander although there is a wide variance in the amount of latitude afforded him. For example, Air Force commanders in the United States have complete discretion as long as some distribution is made to MWR.

Marine Corps' commanders, on the other hand, are required to distribute 85 to 90 percent of total package store profits to the clubs.

DOD-wide, the clubs received \$35 million or 74 percent of the package store profits allocated during fiscal year 1977. Only \$13 million or 26 percent of the profits were transferred to the morale, welfare, and recreation area. Moreover, the benefits from club funds generated by package store sales were, for the most part, limited to those who use the clubs. According to responses to our questionnaire of service members, 24 percent of all eligible personnel never use the clubs, and 44 percent use their club less than once a month. This indicates a significant number of service members are receiving little if any benefits from package store profits distributed to clubs. We concluded, therefore, that the Committee's intent, with respect to the distribution of package store profits, has not been carried out by the Services.

With regard to the need for package store profits, we noted that the Air Force club system in Europe was able to operate successfully without any subsidizations from the package stores. Because of time limitations, we did not determine whether Air Force clubs in Europe are operated more efficiently and effectively than other clubs. We suspect that increased patronage experienced in overseas'

locations contributes to the Air Force's relative success. We believe, however, that this situation demonstrates that clubs can be operated without substantial subsidies.

Appropriated fund support

The club systems collectively lost \$16 million from operations during fiscal year 1977, even though they received \$93 million in "free" personnel, utilities, equipment, and supplies in the form of appropriated fund support. During the fall 1977 hearings held by the Nonappropriated Fund Panel, the Chairman cited the funding of nonappropriated fund activities with appropriated fund support as a major issue confronting the Congress and the executive branch. The Panel felt that total appropriated funding would undoubtedly be objectionable to the taxpayers of this country; complete withdrawal of such support would be "pennywise and pound foolish."

Although we agree with the Services that abrupt withdrawal of appropriated fund support is not feasible, we believe reliance on these funds could eventually be lessened.

Military personnel costs constitute a major portion of appropriated fund support applied to club systems. In our report "Appropriated Fund Support for Nonappropriated Fund and Related Activities in the Department of Defense" (FPCD-77-58, August 31, 1977), we reported that DOD's longstanding policy (Directive 1315.10) of using civilians to the maximum

extent had not been followed for several years. We recommended that the Secretary of Defense revise DOD's policy to authorize military staffing of MWR activities only where civilian employees are not available.

The 1978 Defense Appropriation Bill reduced the number of military personnel that can be used in nonappropriated fund activities. The conference committee directed that DOD emphasize the maximum use of nonappropriated fund civilians instead of military personnel.

Nevertheless, our review showed that in at least three of the Services, the majority of club management positions are still held by military personnel paid with appropriated funds. It should be noted that Navy officials estimate only about 20 percent of its club management positions are held by military personnel and that the Air Force is converting all officers positions in its open mess program to civilians. Again, the continued use of military club managers rather than available civilians is contrary to DOD's own regulations and should be discontinued. Civilianization of management would reduce appropriated fund support as well as eliminate some of the problems associated with military managers, many of whom lack the flexibility and experience to perform their duties in the most effective manner. Our recent report "Military Personnel Cuts Have Not Impaired Most Morale, Welfare, and Recreation Activities" (FPCD-79-54,

July 11, 1979), illustrates how each conversion of an MWR position from military to civilian results in significant savings. A military position converted to an appropriated fund civilian position can save the taxpayers \$5,700; and a military position converted to a nonappropriated fund civilian position can result in savings of almost \$25,000.

In this regard, the Defense Audit Service reported in February 1978 that it identified over 5,300 Army, Air Force, and Marine Corps personnel at 15 military installations who were assigned to provide base support services, or who were detailed to MWR activities. The report concluded that the use of military personnel on special duty for extended periods impacted adversely on the individuals involved and on unit readiness.

Conclusions

We believe alcohol package store profits and appropriated fund support serve as disincentives to achieving efficiencies and economies in operations. These sources of revenue have permitted the club system to operate with complacency rather than with dedication to produce the most effective organization offering maximum services to members.

Under optimum conditions, the military club system should for the most part be self-sustaining, supporting itself with revenue from operations. We recognize that self-sufficiency cannot be accomplished overnight. However,

as greater efficiencies and economies in management and operation are realized, reliance on both package store profits and appropriated fund support could eventually be reduced.

As one of the first steps in reducing the reliance of clubs on package store profits, the administration of and financial reporting for the clubs and package stores should be separated. This is already the case in Army and Air Force club and package store operations in Europe.

We also believe uniform guidelines should be developed regarding the application of package store profits. The profits should generally be applied to other MWR activities which benefit all base personnel. A portion of the profits could be set aside to assist clubs in certain circumstances. For example, the distribution of package store profits could be limited to cover management overhead costs. Package store profits could also be used to help essential financially troubled clubs to break even or finance capital improvements after all reasonable attempts at achieving self-sufficiency have failed. Remaining profits could be used to expand the MWR program or reduce the need for appropriated fund support for these activities.

MEETING THE NEEDS OF
ACTIVE DUTY PERSONNEL

The ability to attract and retain customers is as important for a successful military club system as it is for any viable business in the private sector. In addition to

generating needed revenues, high patronage indicates success in achieving the objectives of the club system--promoting the morale and well-being of service members and contributing to unit identity, esprit de corps, and improved readiness. Low patronage results in financial losses and is symptomatic of the inability of clubs to meet these objectives.

To aid us in determining whether clubs are meeting their objectives, we obtained the views of a sample of servicemen through the use of a questionnaire. We found that 24 percent of eligible personnel never use their club facilities, and 44 percent use them less than once a month. Overall, the responses indicate that military clubs meet the particular needs of certain segments of the military population, who, in general, feel slightly positive about their clubs. Many junior enlisted personnel are attracted by the clubs' low drink prices and entertainment or use them because there are often few other places available. Many officers and, to some extent, senior enlisted personnel feel pressured or obligated to join the clubs but view them as a good place to socialize with their peers.

Even though over one-half of the military personnel use the clubs for these and other reasons, the remainder never use the clubs or use them infrequently because of the reluctance to socialize with military peers or because of poor atmosphere, poor entertainment, unsatisfactory service,

or inconvenient location. Many persons indicated that they would increase their patronage if these aspects of the clubs were improved or eliminated. Except for location and military socializing, club management could correct these negative aspects of club operations and should concentrate its attention on these deficiencies.

Major changes may be needed in the methods in which these services are being offered. Some of these changes may require adjustments in traditional military concepts, particularly those regarding rank separation. Such changes should not be viewed by servicemen as an erosion of benefits. By modifying the structure of unsuccessful clubs on a military installation, eligible personnel will benefit through improving and retaining club services.

Where club patronage falls to such a low level that the operation is no longer viable or where a small patronage base cannot support multiple club facilities, consolidation may offer a reasonable alternative. Consolidation, for administrative purposes or for permitting joint-use of club facilities by various ranks, has been attempted to a limited extent by each of the Services. It does not represent a panacea for all club problems, and may not be appropriate at certain overseas locations where military readiness could be adversely affected. GAO recognizes the need for maintaining military structure and discipline. However, when all

attempts at achieving self-sufficiency have failed, consolidation may present a workable solution. According to our questionnaire respondents, enlisted personnel would generally prefer some form of an "all-ranks" club consolidation rather than higher prices, reduced services, or club closures. Almost one-third of the officers chose consolidation as a viable alternative.

The type of consolidation which works at one installation may not work at another. Each installation has unique characteristics which should be considered. Some of the various alternatives include:

- Opening all club facilities to everyone regardless of rank. Each separate facility could concentrate on a different theme to satisfy varying tastes such as a formal dining room, fast-food operations, and a disco.
- Officers and senior NCOs sharing the same dining room but retaining separate bars.
- Where there is a large club facility, retaining separate dining rooms and bars served by common management and a central kitchen.
- Retaining separate facilities but combining such functions as management, procurement, and accounting.

These are variations of possible consolidations. The important factor that must be considered is to provide adequate and necessary services to all eligible personnel. Although consolidation may involve combined use of facilities by various ranks, overall services offered may actually improve. For example, we reviewed a proposed consolidation of the dining services offered to officers and NCOs at the

Alconbury Air Base which had been rejected by the wing commander. In this instance the officers' club offered no entertainment and was closed on weekends. By permitting the officers to use the NCO facilities, the officers would benefit by being provided services that they now lack. In addition to providing improved services to officers, club management officials estimate that the present \$60,000 loss experienced by the officers and NCO clubs could be converted to a net annual profit of \$68,000.

Conclusions

Based on relatively low patronage and the poor financial condition of many military clubs, we believe the club system may not have adequately adjusted to the changing military environment. As a result, MWR program objectives are not being effectively achieved and tax dollars are being used to support certain club operations with questionable value. Club management must continually consider whether clubs are providing the services required and desired by active duty military personnel. If they are not, the Services must determine how the needs of personnel would be better served. If sufficient commercial facilities are available and can adequately meet these needs or if multiple club facilities on an installation are not supported by base personnel, adjustments in club services may be appropriate. Factors such as club atmosphere, entertainment, and the type of service

offered must be frequently evaluated by club management to ensure that the market is being properly served.

Military clubs at overseas locations are particularly important to American servicemen. These clubs fill a void in the lives of personnel stationed overseas and should provide optimum services to ensure that the quality of life overseas is equal to that enjoyed by personnel stationed in the U.S.

If all reasonable attempts at improvement cannot result in better services and increased patronage, other alternatives must be considered. Where clubs are having financial difficulty resulting in part from a small patronage base, some form of consolidation may present a viable alternative.

NEED TO STRENGTHEN MANAGEMENT OF MILITARY CLUB SYSTEM

The military club system is decentrally managed with overall policymaking and management oversight the responsibility of the Office of the Secretary of Defense (OSD). Each of the four Services has established a separate management and oversight group at the headquarters level to oversee club activities. Day-to-day administration of club activities, however, has been delegated to the installation commanders who are relatively autonomous in operating clubs.

Minimal OSD involvement

We found that OSD involvement in club activities is minimal. One official in the Office of the Assistant

Secretary for Manpower, Reserve Affairs, and Logistics is responsible for monitoring all MWR activities of which clubs are only one component. Without staff, this official is limited to issuing broad policy statements. Data received through the financial reporting system described in DOD Directive 7000.12 is not analyzed for OSD management purposes, although it has the potential for being a useful tool if inaccuracies in the data were corrected. If adequate staff were provided, this official believes his office could more effectively execute its management oversight responsibilities.

Service headquarters' activities ineffective

Each of the four Military Services has established its own headquarters management and oversight functions to administer club and package store activities. The primary mission of these headquarters groups is policy direction. Policy implementation is generally left to installation commanders. The headquarters management groups do not have direct authority over commanders in substantive club matters. This anomaly contributes to a fragmented form of management with base commanders not always acting in the best interest of the clubs.

Local command actions impact adversely on club operations

During our visits to selected military installations, we identified several examples where local command actions

impacted adversely on club operations. Some of the installation commanders on bases we visited demonstrated an inflexible and unbusiness-like approach to club operations. Commanders are inclined to avoid changes in traditional military concepts such as the retention of separate clubs for officers, NCOs, and enlisted personnel, even where a consolidation of facilities would be a viable solution to club problems. Commanders are reluctant to close unprofitable operations and provide for the joint use of clubs by personnel of various ranks although such action would often permit realization of economies of scale and improved service to eligible personnel.

As a substitute for efficient operations, commanders are heavily reliant on package store profits and appropriated fund support. In addition, dues and income from slot machines are also important to club operations. Dependence on these sources of revenue serve as a disincentive to achieving profitability and improving club operations. Commanders are relatively free to accept or reject suggestions for improvement in operations by audit teams and management review groups. Higher command and headquarters officials, however, are reluctant to exert pressure on commanders to implement needed changes because they wish to respect command prerogatives.

Club managers often lack needed flexibility and experience

The club management field presents many challenges and requires talented personnel who are familiar with club operations. They should be well-informed about the market they are required to serve. Of primary importance to successful performance is independence and flexibility to tailor individual club services to the specific needs of installation personnel. Managers also need the latitude and authority to reject ideas that are not workable and not in the best interest of their clubs.

Under the existing club system organization, installation club managers, most of whom are military personnel, are subject to the policies and desires of the installation commanders. The commanders exert considerable influence on the actions of club managers. Yet actions precipitated by the local commanders may not always be in the best interest of the installation club system.

Military rotation policies also prevent managers from acquiring and effectively using valuable general experience in the club management field and specific experience at individual military installations. Military managers are subject to frequent rotation, often to or from an unrelated career specialty. This situation results in a loss of valuable experience and insight into the specific needs of clubs and their patrons at individual military installations.

Conclusions

The management weaknesses I have discussed contribute to the financial difficulties presently confronting the military club system. A strong central management system is needed to provide this significant business-oriented activity with sound direction. Under the existing system, no central authority oversees the operation of the military club system or compares and contrasts the successes and failures of club operations.

We believe that a strong central management system would help ensure that the military club system is administered in a business-like manner and that OSD policies are consistently applied among the Services. Responsibility for club operations should be transferred from installation commanders to a central authority which has the experience and expertise to operate military clubs in an efficient, effective and economical manner.

Strong central management could be achieved through a number of alternatives such as:

- Establishing a strong management authority at the OSD level.
- Establishing a separate DOD club management agency composed of representatives from each of the Services.
- Appointing one of the Services to serve as the executive agent to manage all military clubs.
- Strengthening the present management authorities within each Service and increasing OSD's coordinating and oversight responsibilities.

Under each alternative, installation commanders could continue to serve as management advisors in a central management system to provide valuable suggestions to tailor the services offered on a particular installation to the needs of servicemen. The major policy direction provided club managers should, however, originate at the headquarters' level.

Installation club managers would be able to more effectively administer their clubs if they reported to a higher authority than the local commander. To operate a successful military club, a manager must be completely familiar with the market he is attempting to serve. Although he must operate within the overall framework of military policies and procedures and sound business practices, he must tailor the services offered to the needs of servicemen at each installation. Under the present decentralized system in which managers are subject to the strong and often negative influence of installation commanders, local management's ability to administer club operations effectively is being hindered.

RECOMMENDATIONS

In these times of fiscal constraints, it is particularly important that DOD and the military services recognize the need for greater efficiencies and economies in club and package store operations. We recommend that DOD take steps to improve military club operations to provide

better services to eligible personnel and to achieve eventual financial self-sufficiency. To do this the Secretary of Defense should:

- Strengthen management of the club system by transferring responsibility for club operations from installation commanders to a strong central management authority. A structure consisting of representatives from each Service would ensure that their specific needs receive appropriate attention. Recognizing that such an action will require extensive planning and preparations, we recommend that during the transition the Services transfer responsibility for club operations from the installation commanders to the headquarters authorities and assign club management personnel to these authorities.
- Direct that profits from package store operations be used primarily to support essential MWR activities benefiting all base personnel. Profits distributed to clubs should be limited to helping essential, financially-troubled facilities to break even or finance capital improvements after all reasonable attempts to attain self-sufficiency have failed. These profits could also be used to fund indirect operational expenses associated with the central management authority.
- Direct that package store and club operations be separated as they are by the Army and Air Force in Europe to provide a clearer picture of club operations and package store distributions.
- Direct that dependence on appropriated fund support to clubs be reduced and that the Services civilianize club operations to the maximum extent practicable using nonappropriated funds.
- Direct the Military Services to seriously consider consolidating club services when all attempts at achieving self-sufficiency have proven unsuccessful. Consolidation should be carefully planned and designed to ensure improved services to all eligible personnel.

The Department of Defense has advised the Chairman that it considers our report to be constructive and helpful in