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April 1999

# MILITARY BANKING

## Solicitations, Fees, and Revenue Potential



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**National Security and  
International Affairs Division**

B-281135

April 15, 1999

The Honorable Floyd Spence  
Chairman  
The Honorable Ike Skelton  
Ranking Minority Member  
Committee on Armed Services  
House of Representatives

In your Committee's report on the National Defense Authorization Act for Fiscal Year 1999, you expressed concern about the Department of Defense's (DOD) domestic banking program on military bases and required that we review certain aspects of the program. In response to that mandate, we determined whether (1) domestic military bases have followed DOD procedures to provide for open solicitations in obtaining banking services,<sup>1</sup> (2) on-base financial institutions face competition for banking services from other financial institutions and charge fees competitive with other banks, and (3) opportunities exist for DOD and military bases to generate additional revenues from banking services on military bases and how this might affect banking services and customers.

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**Results in Brief**

In the 15 instances where domestic military bases sought banking services since 1996, the military services openly solicited proposals from financial institutions and selected from among the proposals to authorize a bank or credit union to operate on the base, as required by DOD regulations. Eleven of the solicitations resulted in two or fewer responses. In a few instances where no proposals were received, DOD had to take special action to obtain banking services. We learned of no unsolicited proposals from financial institutions to provide banking services on other bases. When a base received more than one proposal, commanders cited a range of factors on which they based their selection decisions, such as fees, operating hours, or services. The applicable regulations and instructions do not contain specific guidance for this selection process. Further, solicitations did not specify selection criteria or the weights associated with various factors considered. The lack of clear selection criteria makes it difficult to know the basis for selection and ensure fairness in the selection process.

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<sup>1</sup>The general procurement laws do not apply because the bases are not procuring services for the direct benefit of the government and are not using appropriated funds.

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Financial institutions on military bases face significant competition both on and off the base. Less than half of DOD's personnel use an on-base financial institution as their primary banking provider, according to a 1997 DOD survey. On many bases, a bank and a credit union compete for business with each other and with off-base financial institutions. Fees charged by base financial institutions were close to the national average and within the range charged by all banks, on or off base.

A few options exist for potentially generating additional revenues for DOD from financial institutions operating on its bases; how successful such options would be is unclear, and customers and banking services could be adversely affected. First, given that many banks' lease agreements on military bases extend to 25 years, DOD could raise an unknown amount of additional revenue by incorporating in new leases and operating agreements the requirement to periodically renegotiate lease payments based on changes in fair market value, although there is some risk that lease payments might decline. Second, DOD could negotiate automated teller machine (ATM) fee-sharing arrangements, as is sometimes done in the private sector. Third, DOD could competitively solicit ATM placements apart from other banking services. The amount of additional revenues that could be obtained would vary by market conditions, including customers' reactions to likely increases in ATM charges.

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## Background

DOD has arranged for banks and credit unions to operate on military bases for decades, providing convenient banking services for military and civilian personnel assigned there. They also serve official purposes such as disbursing funds or serving as a depository for funds generated by other activities on military bases. According to DOD data, 116 domestic bases have banks and 223 have credit unions, which together field over 1,000 ATMs.<sup>2</sup>

DOD transferred management responsibility for its domestic and overseas banking programs to the Defense Finance and Accounting Service in 1998. The Office of the Under Secretary of Defense (Comptroller), which

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<sup>2</sup>Based on DOD data as of September 1998. We did not validate the data, but we noted that the list included bases targeted to be closed under the base realignment and closure process, and in a few instances omitted base information. Nevertheless, the data appears to provide a general indication of the overall size of DOD's banking program.

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previously managed the programs, now provides policy guidance. Banks on bases are subject to both state and federal regulations.

Procedures that apply to bank operations on military bases in the United States<sup>3</sup> are different from those that apply to such services on bases overseas. In the United States, banks and credit unions typically operate on military bases based on written operating agreements issued under DOD and service policy guidance. In contrast, DOD contracts for overseas banking services under the Federal Acquisition Regulation.<sup>4</sup> (See app. I for information on DOD's overseas banking program.) Military affiliated credit unions chartered in the United States are often permitted to establish branch offices on U.S. military bases in other countries, but they are not under contract with DOD.

No specific statute governs the solicitation and selection of financial institutions to provide a full spectrum of banking or credit union services on domestic military bases.<sup>5</sup> DOD has issued regulations that call for military bases to initially solicit proposals from nearby financial institutions.<sup>6</sup> The military services also solicit nationally, if necessary. DOD regulations delegate authority to the services to prescribe regulations for soliciting financial institutions and selecting the institution making the best offer. According to DOD officials, financial institutions may also submit unsolicited proposals to provide banking services on military bases. As of February 1999, DOD was reviewing and revising its regulations and intended to publish the proposed regulations for comment in the near future.

DOD's regulations currently direct the military services to prescribe procedures for soliciting financial institutions and require that the services review proposals to establish banking offices and select the banking

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<sup>3</sup>Includes the Commonwealth of Puerto Rico.

<sup>4</sup>See 48 C.F.R. chapter 1 (1998).

<sup>5</sup>The Competition in Contracting Act does not apply in this instance because this law applies to the military services' procurement of property and services directly benefiting the government and for which payment is to be made from appropriated funds (10 U.S.C. 2302 et. seq.).

<sup>6</sup>DOD Instruction 1000.12, "Procedures Governing Banking Offices on DOD Installations," as codified at 32 C.F.R. Part 230; DOD Directive 1000.11, "Financial Institutions on DOD Installations," as codified at 32 C.F.R. Part 231; and DOD Instruction 1000.10, "Procedures Governing Credit Unions on DOD Installations," as codified at 32 C.F.R. Part 231a.

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institution making the best offer.<sup>7</sup> These regulations provide general guidance on how financial institutions are to be solicited. The military services' regulations more fully describe how proposals from financial institutions are to be solicited, for example, by contacting nearby institutions and placing advertisements in local newspapers.<sup>8</sup> However, none of the regulations provide guidance on evaluating submitted proposals.

Under DOD regulations, solicitations for banking services originate with individual base commanders' identification of a need for banking services and a request that their service headquarters authorize a solicitation for proposals for a financial institution to operate on the base. Once selected, these financial institutions are required to sign a lease for space and/or an operating agreement specifying their services and fees. Banks are to pay not less than fair market value for space they occupy,<sup>9</sup> while credit unions may occupy facilities without charge under certain conditions.<sup>10</sup> The term of a lease for government-owned facilities generally does not exceed 5 years. Because banks and credit unions may construct buildings on military bases, land lease agreements may be long term, up to 25 years. Banks and credit unions having their own facilities on base reimburse the bases for government-furnished services, including utilities. DOD regulations require that all leases contain a clause that allows DOD to withdraw authorization for cause or because of DOD decisions about base operations such as base closure, deactivation, or substantial realignment.

Within the last 4 years, the Defense Commissary Agency and the Army & Air Force Exchange Service have begun signing agreements with banks and credit unions to operate inside their facilities. In some cases, the financial institutions receive space at no cost in return for helping with cash

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<sup>7</sup>32 C.F.R. 230.4(d)(1) and (2).

<sup>8</sup>The services have issued their own separate regulations: Army Regulation 210-135, "Banks and Credit Unions on Army Installations;" Air Force Instruction 65-701, "Banking Services on Air Force Bases" and Air Force Instruction 65-702, "Credit Unions on Air Force Installations;" and Secretary of Navy Instruction 5381.5A, "Financial Institutions on Navy and Marine Corps Installations."

<sup>9</sup>10 U.S.C. 2667 specifies that all money received under leases entered into by the secretary of a military department shall be deposited in a special account established in the Treasury for the department except amounts paid for utilities and services. Fifty percent of the money deposited in the account is available for facility maintenance and repair or environmental restoration at the base where the leased property is located and 50 percent is for facility maintenance and repair and for environmental restoration by the military department concerned.

<sup>10</sup>Congress specifically authorized this benefit in 12 U.S.C. 1770.

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management activities for retail operations. Leasing issues regarding base involvement in decisions by commissaries and exchanges, including leasing fees, are still under DOD review.

The Conference Report accompanying the 1999 Defense Appropriation Act requires that any bank offering financial services to a base must provide a full range of banking services, including ATMs.<sup>11</sup> This direction is consistent with DOD policy that generally only financial institutions authorized to operate on the base may place ATMs there. Where a base does not have enough personnel to sustain operation of a full service bank, the base commander has the authority to solicit proposals for a sustainable level of financial services, such as ATMs. The domestic banking program does not procure a service for the military and is not financed with appropriated funds, so the general procurement laws do not apply.<sup>12</sup> Consequently, there is no statutory requirement that the selection of domestic banking services be performed on a competitive basis. Likewise, there are no statutory or administrative requirements that, once a financial institution is selected at a particular base, the provision of banking services be recompleted in the future.

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## DOD Openly Solicits Financial Institutions for Banking Services

The military services have conducted 15 solicitations for banking services in the past 3 years. Our review of case files showed that bases followed DOD's procedures requiring open solicitations. However, solicitations during this time drew few responses and in some cases none.

Most of the solicitations since 1996 were for financial institutions that would provide a full range of banking services. In three cases, small bases without banking services requested only ATM service. Our review of case files of recent solicitations for banking services indicates that the military departments solicited proposals from local and national financial institutions where a need for financial services existed because of new requirements or because a bank ceased operations on the base. Table 1 summarizes military departments' solicitations since 1996 and the justification for the solicitation and notes special circumstances about the solicitations.

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<sup>11</sup>House Report 105-746, page 86 (1998).

<sup>12</sup>See 10 U.S.C. 2303(a).

Table 1: Solicitations for Financial Institutions (1996-98)

Service/base	Banking service solicited	Reason for solicitation	Number of proposals received	Comments
<b>Army</b>				
Fort Irwin, Cal.	Bank	New service	0	Base worked with Association of Military Banks of America to identify prospective bank and solicit a proposal.
Arlington Hall National Guard Bureau, Va.	Credit union	New service	2	Two credit unions were eligible to compete based on membership requirements.
U.S. Southern Command, Miami, Fla.	ATM	New service	5	The base selected the offerer with the lowest surcharge for nonaccount holders: \$.75.
Camp Frank D. Merrill, Ga.	ATM	New service	0	One bank expressed interest after the original solicitation closed. The base undertook a new solicitation and received one proposal that it accepted.
<b>Navy/ Marine Corps</b>				
Naval Air Station, Corpus Christi, Tex.	Bank	Bank left	1	The base agreed to provide support to the bank at no cost until it could become profitable.
Naval Training Center, Great Lakes, Ill.	Bank	Bank left	3	The bank not selected filed a protest with GAO, which GAO dismissed because of lack of jurisdiction.
Marine Corps Air Ground Combat Center, Twentynine Palms, Cal.	Bank	Bank left	3	A base selected a local bank, but the bank declined. The base then accepted the proposal rated next highest.
Marine Corps Recruit Depot, Parris Island, S.C.	Bank	Bank left	5	Bank selected agreed to offer special services to the base by providing recruits point of sale cards for purchase of necessities on base during training.
<b>Air Force</b>				
Beale AFB, <sup>a</sup> Cal.	Bank	New service	1	Base solicited banks to operate in the commissary.
Bolling AFB, <sup>a</sup> Washington, D.C.	Bank	Bank left	2	Solicitation was for a bank to operate in the commissary, but Air Force files were incomplete.
Charleston AFB, <sup>a</sup> Charleston, SC	Bank	Bank left	4	Base bank closed operations after a merger. Base solicited banks to operate in the commissary.
Dover AFB, <sup>a</sup> Del.	Bank	Bank left	2	No local banks submitted proposals.
Edwards AFB, <sup>a</sup> Cal.	Bank	Bank left	2	Air Force files were incomplete.
Travis AFB, <sup>a</sup> Cal.	Bank	Bank left	2	Local banks expressed interest but did not submit proposals. Proposals were from national banks.
Will Rogers World Air National Guard Base	ATM	New service	0	No banks or credit unions submitted proposals. The base then signed an agreement with an ATM vendor to provide service in exchange for surcharge revenue.

<sup>a</sup>AFB = Air Force Base.

Source: Our analysis of DOD data.

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As shown in table 1, the services did not receive many proposals in response to a number of the solicitations. In three cases—Fort Irwin and Travis Air Force Base in California and Dover Air Force Base in Delaware—solicitations to local financial institutions did not elicit responses, but banks from out of the area responded. At Fort Irwin, initial solicitations to nine local financial institutions did not produce any proposals, so the Army advertised through the Association of Military Banks of America, a trade association of on-base banks, and received one proposal.

The small number of proposals received through broad, nationwide solicitations indicates that banks do not see on-base operations as very profitable, especially where bases are small or in remote locations. Most of DOD's recent solicitations were to fill voids created when banks left bases, according to DOD officials. In some cases, base banks were taken over in mergers, and the new management decided to stop on-base operations. This was the situation Fort Myer, Virginia, faced in 1994 when the new owner of the on-base bank ceased its operation, turning over its building to the base. Because DOD's solicitation did not result in any proposals, DOD worked with the Association of Military Banks of America to find a bank willing to operate on the base. As an incentive, the base agreed to provide facilities and logistical support at no cost for several years, although the bank hopes to attain profitability and begin paying leasing and operations fees within 2 years.

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### Selection Criteria Not Clearly Stated

While DOD and military service regulations provide guidance as to solicitation procedures, they do not specify factors that base commanders should use to select a financial institution or state the weight that should be given to each factor. DOD regulations simply state that the bank making the "best offer" is to be selected. Our file review indicated that base commanders selected from among proposals based on distinguishing factors such as fees, hours, and range of services. We also noted that there is no criteria to guide banks in preparing proposals. While solicitation letters indicated in general the types of services the financial institutions would be expected to provide, they did not clearly state the relative importance of each requirement. The Army has developed a standardized procedure for evaluating proposals that includes developing weighted factors that define the importance of each criterion for a particular solicitation. Additional clarity in stating the selection criteria would help financial institutions tailor their proposals to meet the installations' priorities and ensure fairness in the selection process.

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## Base Financial Institutions and Fees Are Competitive With Off-Base Banks

Our analysis shows that financial institutions on bases face competition from several sources, both on and off the base. Moreover, a 1997 DOD survey indicates that DOD personnel were satisfied with banking services both on and off base. Our comparison of data on fees charged by banks and credit unions indicates that fees charged on bases were within the range of fees charged by all commercial banks.

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## Financial Institutions Face Competition on and off Bases

DOD generally limits financial institutions on each base to one bank and one credit union. According to DOD and service officials, this arrangement provides competition between the two types of financial institutions. DOD's data indicates that over 100 bases have both a bank and a credit union, and over 100 more have only a credit union. On the bases we visited, bank and credit unions offered similar services and provided a choice to base personnel.

Bases with both banks and credit unions vary in size from about 1,800 personnel to over 50,000. Most large bases have both a credit union and a bank: 29 of 33 bases (88 percent) with more than 15,000 military and civilian personnel had two financial institutions. Smaller bases less frequently had two institutions on base: 61 percent of bases with 5,000 to 15,000 personnel and 31 percent of bases with 1,000 to 5,000 personnel had both a bank and a credit union. None of the 14 bases with fewer than 1,000 personnel had two institutions on base. The largest bases have populations that might support more than two full service financial institutions. However, DOD officials told us that they did not believe that most bases could support more than two financial institutions.

Military personnel and DOD civilians also have many off-base alternatives to the base financial institutions. In most cases, there are banks in communities near bases where many DOD military and civilian employees live. According to DOD officials, most servicemembers who live on bases have transportation options that make it possible for them to bank with financial institutions in the local area if they choose. The growth in electronic and telephone banking has provided additional competition for on-base banks because remote banking services are conveniently accessible.

Available data suggests that DOD personnel were satisfied with the banking facility they used most often whether they banked on or off the base. In DOD's 1997 survey of military and DOD civilian employees, a large majority

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(89 percent) of the 8,403 U.S.-based survey respondents reported that they were satisfied or very satisfied with the financial institution they used most often.<sup>13</sup> Of the U.S.-based respondents who used an on-base financial institution on their current base most often, 88 percent said they were satisfied or very satisfied. Only 37 percent of the respondents said that the financial institution they used most often was a bank or credit union on the base to which they were assigned. About 8 percent of the respondents named the on-base bank as the financial institution they used most often, while 29 percent named the on-base credit union. The largest percentage of respondents (about 35 percent) reported that they most often used a bank not on a military base.

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## Fees Charged Are Similar Both on and off Bases

Fees charged by on-base financial institutions were within the range of those charged by all banks. According to DOD procedures, on-base banks' fees may not exceed customary fees charged for off-base operations. We reviewed data collected by the Federal Reserve Board in June 1997<sup>14</sup> and compared the data with data DOD collected (in August 1998) on financial institutions on bases. We found that the average ATM fees for military banks for which data were available were close to the average of all banks. The average ATM fees for credit unions were less than the average of all banks. However, banks and, with one exception, credit unions on bases charged higher fees for customers that had insufficient funds in their accounts than the national average, although the range of charges on bases was within the range of all banks.

## ATM Fees

Banks and credit unions on bases, like those off bases, generally do not charge their own account holders or members to use ATMs they own. The Federal Reserve Board reported in its June 1998 report that less than 8 percent of all banks charge their account holders for the use of ATMs the banks own. According to a 1998 financial survey by the Armed Forces Financial Network, 11 percent of military households reported paying a fee to use their financial institutions' ATMs. However, according to the data on ATM charges at 118 banks and 175 credit unions on military bases we collected during this review, only two banks (1 percent) and no credit

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<sup>13</sup>The 1997 DOD Financial Services Survey: A Study for the Office of the Under Secretary of Defense (Comptroller), Defense Manpower Data Center, DMDC Report No. 98-008, September 1998.

<sup>14</sup>Annual Report to the Congress on Retail Fees and Services of Depository Institutions, Board of Governors of the Federal Reserve System, June 1998.

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unions charged their account holders or members any fees to use their ATMs.<sup>15</sup>

Most banks on bases impose surcharges or fees for nonaccount holders' or nonmembers' use of the ATMs they own, as do most commercial banks. We reported that 64 percent of banks that operated ATMs as of February 1, 1998, assessed surcharges on at least some of their ATMs.<sup>16</sup> We also reported that in February 1998 the average surcharge for all banks with surcharges was \$1.27. In comparison, 91 percent of banks on bases we reviewed assessed ATM surcharges on nonaccount holders and the average surcharge was \$1.19. Credit unions on bases less frequently charge nonmembers that use their ATMs, but for the 29 percent that did, the average charge was \$1.03. Table 2 shows the average and range of ATM fees and the percent of financial institutions on military bases charging nonaccount holders.

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<sup>15</sup>Our sample included banks located on military bases from each service.

<sup>16</sup>Automated Teller Machines: Survey Results Indicate Banks' Surcharge Fees Have Increased (GAO/GGD-98-101, Apr. 24, 1998).

**Table 2: Charges for ATM Use by Nonaccount Holders or Nonmembers on Military Bases**

<b>Service</b>	<b>Characteristic</b>	<b>Bank</b>	<b>Credit union</b>
<b>Army</b>	Mean	\$1.17	\$1.07
	Range	\$0-2.00	\$0-2.00
	Percent charging a fee	93	46
<b>Navy</b>	Mean	\$1.17	\$0.78
	Range	\$0.45 to 2.00	\$0-1.00
	Percent charging a fee	100	3
<b>Marine Corps</b>	Mean	\$1.14	\$1.10
	Range	\$0-1.50	\$0-1.50
	Percent charging a fee	78	31
<b>Air Force</b>	Mean	\$1.23	\$0.97
	Range	\$0-2.00	\$0-1.50
	Percent charging a fee	88	48
<b>All services</b>	Mean	\$1.19	\$1.03
	Range	\$0-2.00	\$0-2.00
	Percent charging a fee	91	29

Note: The means presented refer to banks that assess surcharges but not to banks that do not assess surcharges; the range and percent refer to the whole sample.

Source: Our analysis of data provided by the services.

Most banks assess their account holders a charge to use an ATM owned by another bank, as do most financial institutions on bases. Fees charged by banks nationally ranged from \$0.25 to \$2.00 and averaged \$1.14 in 1997, according to the Federal Reserve Board study. Fees charged by banks on bases ranged from \$0.45 to \$2.00 and averaged \$1.20. Just over half of credit unions charged a fee that averaged \$0.94. Table 3 shows the average, range, and percent of fees charged to account holders of banks and credit unions on military bases that use other financial institutions' ATMs.

**Table 3: Charges by Banks and Credit Unions for Their Account Holders' or Members' Use of an ATM Owned by Another ATM Provider**

Service	Characteristic	Bank	Credit union
<b>Army</b>	Mean	\$1.21	\$1.04
	Range	\$0-2.00	0-2.00
	Percent charging a fee	93	57
<b>Navy</b>	Mean	\$1.06	\$0.77
	Range	\$0-1.50	\$0-1.00
	Percent charging a fee	94	32
<b>Marine Corps</b>	Mean	\$1.36	\$0.86
	Range	\$0-1.50	\$0-1.00
	Percent charging a fee	78	94
<b>Air Force</b>	Mean	\$1.24	\$0.99
	Range	\$0-2.00	\$0-1.00
	Percent charging a fee	92	61
<b>All services</b>	Mean	\$1.20	\$.94
	Range	\$0-2.00	\$0-2.00
	Percent charging a fee	93	51

Note: The means presented refer to banks that assess surcharges but not to banks that do not assess surcharges; the range and percent refer to the entire sample.

Source: Our analysis of data provided by the services.

## Other Fees

On-base banks' average fee for a check returned for insufficient funds was higher (\$19.93) than the average of all banks (\$16.55) according to Federal Reserve data. The insufficient funds charges by banks on bases ranged from \$8 to \$29 compared to all banks' range of \$5 to \$30. The average charge by credit unions on bases was \$17.41 and ranged from \$10.00 to \$35.00. Returned check charges by all banks and, with one exception, credit unions on military bases fell within the range of charges the Federal Reserve Board found.

Although the Federal Reserve Board study provided no average fees for money orders, we found that banks and credit unions on bases most typically charged \$1.00 for this service. Charges by banks on bases averaged \$2.16 and ranged between \$0.50 and \$5.00. In comparison, charges at base credit unions averaged \$1.17 and ranged from \$0.00 to \$6.00.

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## Potential for Raising Revenue From Base Financial Institutions Is Uncertain

To respond to the mandate to examine options for generating revenues from financial institutions, we identified three options DOD could examine to potentially raise additional revenue from financial institutions operating on military bases: (1) increase lease charges; (2) seek to share revenues banks receive through service fees, such as ATM fees; or (3) competitively solicit bases for ATM placements apart from other banking services.<sup>17</sup> These options may require changes in the rules that now govern banking on military bases. The precise impact of these actions on the quality of life on military bases is uncertain. Some financial institutions operating on the bases might be able to afford higher payments than they currently make, while others might not. The recent history of banks leaving bases due to low profits suggests that additional fees might further reduce the attractiveness of on-base operations.

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## Adjusting Current Lease Fees Based on Fair-Market Value

Since 1991, 10 U.S.C. 2667 has required that banks pay in cash or in kind not less than fair market value for the use of government-owned land or facilities on military bases.<sup>18</sup> To increase its revenues, DOD could change future lease and operating agreements to provide for periodically reviewing and adjusting lease fees based on changes in fair market value.

Under current procedures, lease charges for financial institutions remain constant through the life of lease agreements—up to 25 years. According to service officials, banks that signed leases before 1992 pay a nominal fee through the term of their leases, in accordance with regulations in effect before 1992. Banks that signed leases after 1992 pay the current fair market value for the term of their leases. DOD could change its procedures to include a recurring assessment of fair market value on long-term leases to ensure that banks' leases reflect current conditions. Neither the Army Corps of Engineers, which determines fair market value for Army and Air Force bases, nor the Navy's Engineering Division, which determines fair

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<sup>17</sup> 10 U.S.C. 2667(d) requires military departments to deposit any money received from rentals into a special account in the Treasury to be used for certain purposes, such as facility maintenance and repair. Any other moneys received must be deposited into the Treasury as miscellaneous receipts (31 U.S.C. 3302(b)) unless otherwise authorized by law.

<sup>18</sup> In some cases, DOD may provide facilities and operating support, such as utilities, at no cost to banks based on their profitability. At the time of our review, three banks received facilities and operating support at no cost. These banks were located on Fort Myer, Virginia; the Naval Air Station, Meridian, Mississippi; and the Naval Air Station, Corpus Christi, Texas.

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market value for Navy and Marine Corps bases, currently have regulations that require periodic reviews of fair market value.

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### Fee Sharing of ATM-Related Surcharges

DOD does not currently assess any fees that are dependent on financial institutions' revenues from banking operations on military bases, and it is unlikely that financial institutions would readily share such information with DOD. To raise revenues, DOD could implement a fee-sharing arrangement related to ATM surcharges.

The profitability of ATMs depends on the number of transactions they make—particularly transactions for nonaccount holders that pay a surcharge. Banking officials said that banks in the private sector sometimes pay set amounts and/or enter into fee-sharing arrangements to place ATMs in high-traffic locations such as grocery stores and airports. According to these officials, this practice varies according to the desirability of the location, based on access to customers and potential customers' alternatives for obtaining cash.

Officials of banks and credit unions now authorized to operate on bases said that their current placement of ATMs is not necessarily driven by direct profits from individual ATMs. They said they serve the base community by providing ATMs that are convenient for the military community, for example, in barracks and at remote training sites, but are not very profitable. Often, base officials ask banks or credit unions to place ATMs in locations to benefit the base community. For example, officials at the Marine Corps Base at Quantico, Virginia, asked the base credit union to support an ATM at its bachelor officers' quarters. The credit union complied, although a credit union representative reported that the ATM does not produce large profits.

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### Competition for ATM Placements

A related option to raise revenue for DOD might be to competitively solicit placement of ATM operations on military bases apart from full service banking operations. This option might generate revenue by requiring that ATM sponsors pay a flat fee or a percentage of revenues from transactions to DOD. Some ATM vending companies might be willing to pay to locate ATMs in prime locations on military bases. Some banking representatives stated that increased competition through representation of additional financial institutions would raise money for bases. Of the 15 recent solicitations DOD conducted, three involved solicitations for ATM service only. In one case, the base was small and remote, and the base initially

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received no proposals. In another, the base was a headquarters office building located in an urban area and received five proposals. In the third case, a base that received no proposals entered into an agreement with an ATM vendor to provide ATM service in return for 30 percent of the surcharge revenue. DOD's preference is to obtain full-service banking on its bases where feasible so that DOD personnel will have convenient access to a range of banking services and financial counseling.

The amount of revenue that could be raised by soliciting bids to provide ATMs would depend on how financial institutions valued selected sites on individual bases. While ATM vendors might be willing to pay to locate ATMs in high foot-traffic areas, according to DOD banking officials, it is unlikely that vendors would support ATMs at less popular locations without a high surcharge. DOD officials expressed concern about the potential negative impact of separating the provision of ATM services from its full service banking program. In a report to the House Committee on Appropriations on competitive banking procedures, DOD said that the only way stand-alone ATMs would create significant revenues for DOD would be by levying substantial new ATM surcharges on DOD military personnel and their families.<sup>19</sup> According to this report, such a charge would most negatively affect junior-grade enlisted personnel because they are least able to afford surcharges imposed on the use of ATMs. Further, the report stated that the adverse financial consequences on individual servicemembers would outweigh any benefits to DOD.

While this option might raise some revenue for DOD, it conflicts with DOD's current policy of granting exclusive rights for ATMs to its on-base financial institutions. It might make on-base operations less attractive and further erode the full-service banking capability DOD seeks. In addition, this option would be inconsistent with the direction in the Conference Report accompanying the 1999 Defense Appropriation Act that any bank offering financial services on an installation must provide a full range of banking services.

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### Impact of Efforts to Increase Fees Could Vary by Base

It is difficult to forecast in advance precisely what effects would result from efforts to increase revenues generated for DOD from banks and credit unions operating on military bases. Much would likely depend on the profitability of existing operations. In some situations financial institutions

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<sup>19</sup> Department of Defense, Report on Competitive Banking Procedures, September 17, 1998.

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might be expected to increase fees to try to make up the difference in their profits, with their customers bearing the additional costs. In some situations, banks might decide to cease operations on bases, as some have done in the past based on concerns over profitability.

Faced with higher fees, some current on-base bank customers might take their accounts to other financial institutions with lower fees, either on or off base. In its 1997 financial survey, DOD found that low prices were a major factor in choosing a financial institution for most respondents. In a 1998 survey conducted for the Armed Forces Financial Network, a sizeable majority (78 percent) of DOD respondents reported that they would change their current behavior to avoid ATM fees and would not use an ATM where they were charged \$2 or more.<sup>20</sup>

DOD officials and representatives of financial institutions on military bases told us that because the number of people with access to on-base bank and credit union facilities is limited, the profitability and stability of current on-base financial institutions could be at risk if their net revenues were decreased by increases in operating costs. In some cases, according to DOD and banking officials, banks and credit unions would probably leave their on-base locations if operating costs increased. If banks that hold bases' Treasury general accounts<sup>21</sup> left, the bases' costs to obtain these services would increase.

Of the three options, the one that would provide competitive placement of ATMs on bases apart from other banking services would likely have the greatest impact on current banking operations. The on-base financial institutions that currently provide ATM service would incur additional costs to provide the service or would lose access to the most potentially profitable locations—those likely to be bid on by off-base ATM vendors. Both outcomes would decrease revenues for institutions currently on bases—potentially causing them to leave the base.

In its report to Congress on competitive banking procedures, DOD stated that the loss of an on-base bank has historically been detrimental to

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<sup>20</sup>The Armed Forces Financial Network is a provider of networking capability jointly sponsored by the Association of Military Banks of America and the Defense Credit Union Council.

<sup>21</sup>The Department of the Treasury establishes Treasury general account relationships with financial institutions so that federal program agencies will have access to efficient and effective systems for the management of public funds.

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productivity because assigned personnel must travel off base to obtain financial services. In addition, on-base entities such as DOD disbursing officers, commissaries, and nonappropriated fund instrumentalities would incur additional costs to meet their banking needs. DOD officials expressed further concern that revenue generated by separate vendor-offered ATM services might not be sufficient to offset the additional costs to DOD due to the loss of on-base banks.

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## Conclusions

When needs for banking services have arisen, the services have publicly solicited proposals from banks and credit unions. We found that solicitations often indicate factors important to the bases in selecting from among proposals, and selecting officials cited varying factors influencing their selections; however, we could not determine the importance and weight of each criterion in the selection process for each solicitation. Better identification of the selection criteria and the relative importance of each criterion could be useful in enhancing proposals received and fostering greater assurance of fairness in the selection process.

Banking service fees on military bases appear to be within the range of charges found at banks nationally, although some fees appear to be higher than national averages.

DOD could ensure it continues to receive fair market value for use of its facilities by financial institutions by periodically reassessing the fair market value associated with long-term leases. However, lease fees could decrease if property values decrease. DOD could also negotiate some type of fee-sharing arrangement for ATM services. The extent to which higher costs would be absorbed by financial institutions, be passed onto customers, or affect the financial institutions' willingness to provide services on military bases is uncertain and likely to vary based on the characteristics of individual bases. However, an adverse impact on customers or services could result if financial institutions raise their fees to cover operating costs or leave the base.

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## Recommendations

We recommend that the Secretary of Defense direct that forthcoming regulations governing banking on military bases require base commanders to ensure that solicitations for banking services include information on factors and weights to be used in choosing among competing proposals and

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that the evaluation of proposals and the selection of on-base financial institutions be based on those factors and weights.

We also recommend that the secretaries of the military departments consider including in new long-term lease arrangements provisions for periodically renegotiating fees based on updated fair market value to better ensure that the government is obtaining payments commensurate with the current value of the property.

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## Agency Comments

In written comments on a draft of this report, DOD concurred with both of our recommendations. DOD said that its goal is to ensure that bank and credit union services are available at reasonable cost to DOD personnel on bases. DOD said that it would include provisions on evaluation factors and weights in revised regulations on solicitations currently under review. DOD also said it would request that the military departments review their policies and procedures to consider including in long-term leases periodic renegotiation of fees. In commenting on the draft of this report, DOD stated that it does not support any initiative that would levy additional fees or charges for financial services on DOD personnel to generate or increase revenue for an installation or other organization. DOD's comments are reprinted in appendix II. Appendix III sets forth the objectives, scope, and methodology of our review.

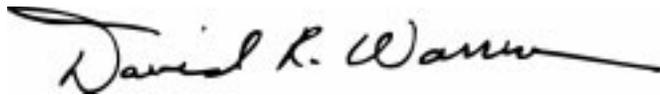
We conducted our review between August 1998 and March 1999 in accordance with generally accepted government auditing standards.

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We are sending copies of this report to Senator John Warner, Chairman, and Senator Carl Levin, Ranking Minority Member, Senate Committee on Armed Services. We are also sending copies of this report to the Honorable William S. Cohen, Secretary of Defense; the Honorable William J. Lynn, Under Secretary of Defense (Comptroller); the Honorable F. Whitten Peters, Acting Secretary of the Air Force; the Honorable Louis Caldera, Secretary of the Army; the Honorable Richard Danzig, Secretary of the Navy; the Honorable Gary W. Amlin, Director, Defense Finance and Accounting Service; and the Honorable Jacob J. Lew, Director, Office of Management and Budget. Copies will also be made available to others upon request.

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Please contact me at (202) 512-8412 if you or members of your staff have any questions concerning this report. Major contributors to this report are listed in appendix IV.

A handwritten signature in black ink that reads "David R. Warren". The signature is written in a cursive style with a long horizontal flourish at the end.

David R. Warren, Director  
Defense Management Issues

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# Contents

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Letter	1
Appendix I DOD's Overseas Banking Program	22
Appendix II Comments From the Department of Defense	23
Appendix III Objectives, Scope, and Methodology	25
Appendix IV Major Contributors to This Report	28
Tables	
Table 1: Solicitations for Financial Institutions (1996-98)	6
Table 2: Charges for ATM Use by Nonaccount Holders or Nonmembers on Military Bases	11
Table 3: Charges by Banks and Credit Unions for Their Account Holders' or Members' Use of an ATM Owned by Another ATM Provider	12

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## Abbreviations

ATM	automated teller machine
DOD	Department of Defense

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**Contents**

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# DOD's Overseas Banking Program

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The process for selecting commercial banks to operate on military bases varies between U.S. domestic and overseas bases. Unlike commercial banks that operate on domestic military bases under lease arrangements and operating agreements with individual bases, the Department of Defense (DOD) uses a formal contract with a single U.S. bank to provide services to multiple locations overseas. Such contracts are awarded on a cost-plus-fixed-fee basis to provide DOD personnel banking services similar to those they could obtain in the United States.<sup>1</sup> DOD may establish overseas banks where allowed by bilateral agreements and host country laws.

Currently, DOD supports banking facilities at 114 locations in Germany, the Netherlands, the United Kingdom, Iceland, Japan, Okinawa, South Korea, Diego Garcia, and Panama. Facilities and logistical support for overseas banking services are provided by the host component commands. DOD specifies fees charged for banking services.

DOD awarded the current contract for overseas banking to NationsBank of Texas. The contract's term is 5 years, from October 1995 through September 30, 2000, and the bank is to provide a range of services at fees and locations DOD specifies. The total cost of the contract, including costs and fees, is estimated at \$500 million. Fees charged to customers offset the major portion of the costs, but the services also obligate appropriated funds that, according to DOD officials, cover the fixed contract fee, bad debts, and operating losses. In fiscal year 1998, the services provided \$11 million in appropriated funds.

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<sup>1</sup>Credit unions on domestic bases have in some instances established branches on overseas bases, but these are not under contract with DOD.

# Comments From the Department of Defense



## DEFENSE FINANCE AND ACCOUNTING SERVICE

1931 JEFFERSON DAVIS HIGHWAY  
ARLINGTON, VA 22240-5291

MAR 22 1999

Mr. David Warren  
Director, Defense Management Issues  
National Security and International Affairs Division  
U.S. General Accounting Office  
Washington, DC 20548

Dear Mr. Warren:

This is the Department of Defense (DoD) response to the General Accounting Office (GAO) draft report, "MILITARY BANKING: Solicitations, Fees, and Revenue Potential", dated February 16, 1999 (GAO Code 709372/ OSD Case 1753).

The DoD concurs with the overall comments and recommendations in the report. Specific comments on the recommendations are attached. Our goal in the military banking area is to ensure that bank and credit union services are available on-base to our personnel at reasonable cost. As your report notes, it is becoming more and more difficult to attract and retain financial institutions on our bases. We do not support any initiative that would levy additional fees or charges for financial services on our personnel.

Thank you for the opportunity to comment on this report.

Sincerely,

A handwritten signature in cursive script that reads "Gary W. Amlin, for".

Gary W. Amlin  
Director

Attachment:  
As stated

GAO Draft Report - Dated February 16, 1999  
(GAO Code 709372) OSD Case 1753

"MILITARY BANKING: Solicitations, Fees, and Revenue Potential"

RECOMMENDATIONS

- **RECOMMENDATION 1:** The GAO recommended that Secretary of Defense direct that forthcoming regulations governing banking on military bases provide guidance to base commanders to ensure that (1) solicitations for banking services include information on factors and weights to be used in choosing among competing proposals and (2) the evaluation of proposals and selection of on-base financial institutions be based on those factors and weights. (p. 24/GAO Draft Report)
- **DOD RESPONSE:** Concur. DoD is currently in the process of revising DoD Instructions 1000.10 and 1000.12 on Credit Unions and Banks, respectively, and incorporating these Instructions into the DoD Financial Management Regulation (DoDFMR). The revised DoDFMR will include provisions on evaluation factors and weights and provide for the use of these factors and weights in the evaluation of proposals received. These revised regulations are currently being coordinated within DoD and will be published in the Federal Register for public comments prior to implementation. Final publication is dependent on many variables in the comment and final coordination process, but is not expected to occur before late summer 1999.
- **RECOMMENDATION 2:** The GAO recommended that the secretaries of the military departments consider including in new long-term lease arrangements provisions for periodically renegotiating fees based on updated fair market value conditions to better ensure the government is obtaining payments commensurate with the current value of the property. (p. 24/GAO Draft Report)
- **DOD RESPONSE:** Concur. The Defense Finance and Accounting Service (DFAS) will request the military departments review their policy/procedures to consider including in new long-term lease arrangements provisions for periodically renegotiating fees and to notify DFAS as to the results of their considerations.

Now on pp. 17-18.

Now on p. 18.

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# Objectives, Scope, and Methodology

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In the House Armed Services Committee (formerly National Security) report on the National Defense Authorization Act for Fiscal Year 1999, we were directed to review certain aspects of DOD's military banking program.<sup>1</sup> Accordingly, we determined whether (1) domestic military bases have followed DOD procedures to provide for open solicitations in obtaining banking services; (2) on-base financial institutions face competition for banking services from other financial institutions and charge fees competitive with other banks; and (3) opportunities exist for DOD and military bases to generate additional revenue banking services on military bases and how this might affect banking services and customers.

To review DOD's selection procedures for banking services for domestic bases, we examined DOD regulations and the military departments' implementing instructions governing solicitation of financial institutions. We also met with officials of DOD's Office of the Under Secretary of Defense (Comptroller) who have policy oversight of DOD banking issues to discuss the history of banking on military bases and DOD's ongoing review of the banking regulations. We also met with officials from the Defense Finance and Accounting Service who have operational oversight of both overseas and domestic banking programs to obtain information about the differences between the two programs. In addition, we met with banking liaison personnel from the Air Force, the Army, the Navy, and the Marine Corps to discuss the status of banking on military bases and the services' solicitation processes. We reviewed the case files of recent solicitations that were available to verify whether the military departments openly solicited proposals for banking services and selected from among the proposals. The solicitation files did not contain proposals from banks that were not selected. Therefore, we did not review the services' evaluations of all proposals they received. Solicitation files for two Air Force bases that had recent proposals were incomplete.

To identify the extent of competition for on-base financial institutions we (1) matched a list of banks and credit unions on military installations provided by DOD with information on base size from DOD's Base Structure Report for fiscal year 1996<sup>2</sup> and (2) met with DOD officials and representatives of on-base banks and credit unions at four military bases—Fort Myer, Virginia; Bolling Air Force Base, Washington, D.C.; Fort Belvoir,

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<sup>1</sup>House Report 105-532 at page 281(1998).

<sup>2</sup>Where installations with financial institutions were not in the base structure report, we obtained information on base size from service officials.

Virginia; and Marine Corps Base Quantico, Virginia—to discuss whether financial institutions on military bases face competition and the sources of that competition. We also discussed these issues with representatives of the Association of Military Banks of America and the Defense Credit Union Council. We reviewed “The DOD 1997 Financial Services Survey” and the Armed Forces Financial Network’s “1998 Survey of Armed Forces Consumers Financial Services Needs and Behaviors” to obtain information about where military consumers obtain their banking services and their satisfaction with these services.

To determine whether banking service fees charged by financial institutions on bases are competitive, we analyzed data from several sources. First, we analyzed data DOD had collected from 46 banks and 86 credit unions to respond to congressional questions on fees for selected services charged by financial institutions on military bases. Not all DOD bases were represented in the information DOD provided, but DOD officials said it represented a fair sample of charges. We compared average fees from this sample of banks with those for similar services charged by all banks, as reported to the Federal Reserve Board. Although DOD information was reported about 1 year after the Federal Reserve Board reported information, the Federal Reserve Board provides a conservative comparison point for charges on military bases.

We also reviewed financial institutions’ charges for on-base ATM service, including service to persons not having an account or membership with the institutions. To obtain this information, we asked the services to provide, for each base, the charges for ATM service for (1) account holders using the financial institutions’ own ATMs, (2) account holders using ATMs owned by another financial institution, and (3) nonaccount holders using the ATMs on bases. We analyzed this data and compared the on-base ATM fees with those from a sample of all banks we reported on in February 1998. We also collected fee information from bases we visited to confirm the accuracy of data DOD provided.

To assess the potential for generating additional revenue from financial institutions and possible impacts on the military community if additional revenues were generated, we interviewed DOD officials and military banking representatives to discuss options for generating additional revenue from financial institutions on military bases and consequences that might occur if these options were exercised. We met with officials from the bases we visited and discussed leasing practices with the Army Corps of Engineers and the Naval Facilities Engineering Command. We discussed

revenue that DOD is currently receiving and obtained documentation regarding lease fees and other payments that DOD collects from financial institutions. We discussed the impacts of potential revenue-raising options with banking representatives at the bases we visited and with industry representatives. We also discussed in-store banking facilities with representatives of banks and credit unions on bases and the Defense Commissary Agency and the Army & Air Force Exchange Service. We also discussed electronic banking issues with representatives of banks not on military bases to obtain information about how remote ATMs are placed at commercial sites.

# Major Contributors to This Report

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