

DEFENSE COMMISSARY AGENCY

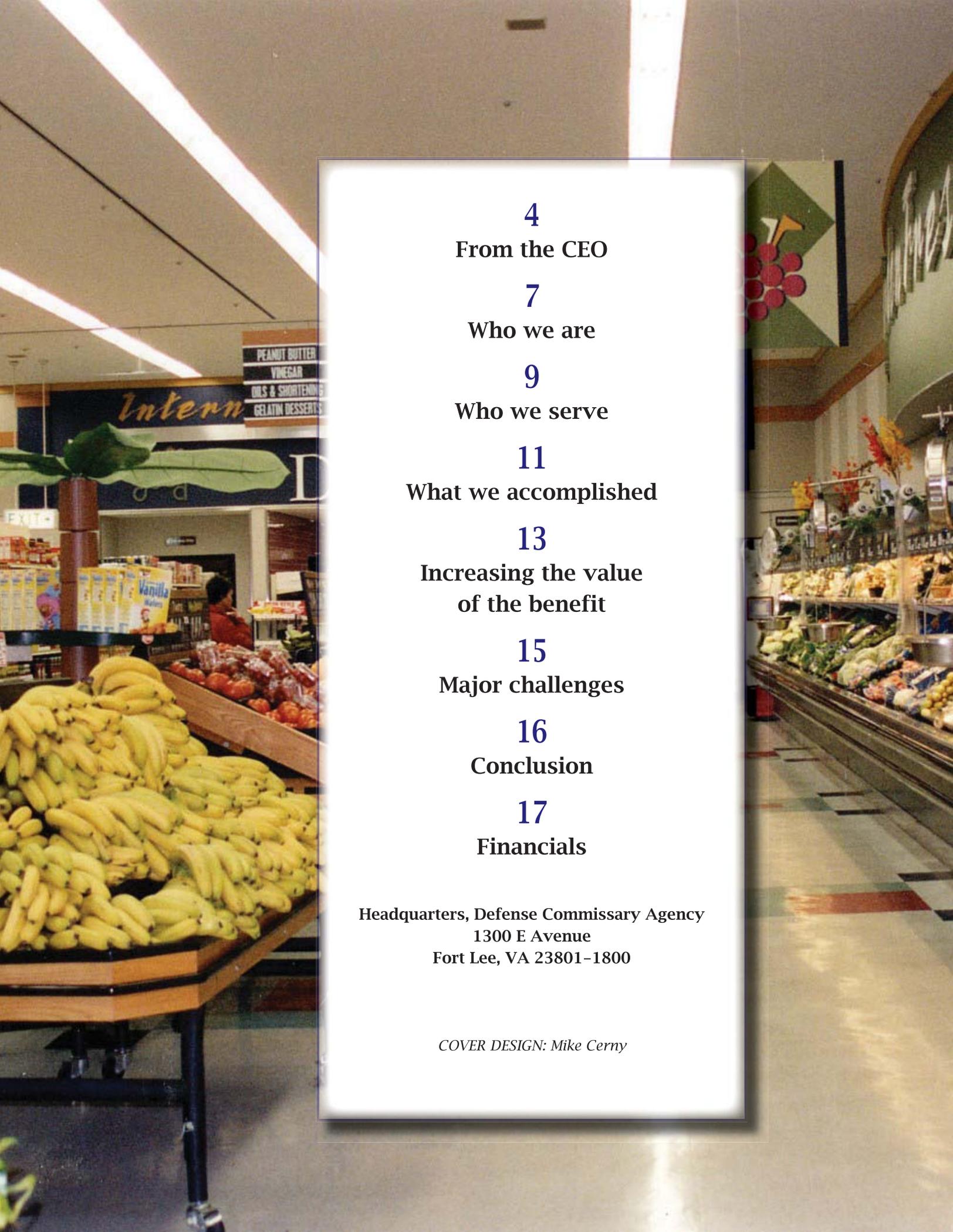
Annual
Report
2005



Our Mission

Deliver a premier commissary benefit to the armed services community that ...

- **Encourages an exciting shopping experience;**
- **Satisfies customer demand for quality grocery and household products; and**
- **Delivers exceptional savings while ...**
 - **Enhancing quality of life;**
 - **Fostering recruitment, retention and readiness; and**
 - **Supporting warfighters' peace of mind, knowing their families have secure and affordable access to American products.**



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**Headquarters, Defense Commissary Agency
1300 E Avenue
Fort Lee, VA 23801-1800**

COVER DESIGN: Mike Cerny

From the Director ...

FISCAL 2005 was another impressive year for the Defense Commissary Agency. It was a year marked by challenge and success in the areas of sales, patron savings, customer satisfaction, resource management, systems modernization and corporate re-engineering, to name but a few.

When all was said and done, the numbers spoke for themselves – sales were up, costs were down, customer satisfaction ratings rose even higher and customer savings remained constant.

Sales up; costs down

While sales growth in the commercial supermarket sector continued to lag, our sales were up 2.5 percent, coming in at \$5.36 billion. At the same time, our costs came in under program, while we continued to deliver savings of 32 percent to our patrons — thanks in no small part to the support of our trading partners without which this wouldn't have been possible. It is this level of savings and the fact that we can deliver it to all of our locations worldwide that make the commissary one of the military's most-valued benefits.

As for customer service, we can say with confidence that our patrons like what we do, as evidenced by the overall 4.55 rating (on a scale of 1 to 5) we received from them on the annual Commissary Customer Service Survey — exceeding our fiscal 2005 goal by 2 percent.

We are also understandably proud of our demonstrated fiscal responsibility in that for the fourth year in a row, independent auditors have given our financial statements an unqualified opinion.

It is performance results like these that make it possible for us to set a self-imposed goal of increasing the value of the benefit without increasing its cost.



JAMES KEGLEY

Patrick B. Nixon

While sales, savings, and customer satisfaction remained strong, the real story behind our sustained excellence has been our evolution into a more efficient and effective organization. We have achieved this through the creativity and dedication of our employees and managers, the course laid out by our strategic planners, the support of those in the Pentagon and on Capitol Hill, the implementation of new technology and best business practices, the streamlining and improvement of our business processes using Lean Six Sigma, and an aggressive outreach program that is delivering the benefit to all segments of our customer base.

Looking back on our accomplishments over the past year, we in DeCA are justifiably proud of the contributions we have made to the quality of life of our nation's military and their families, and we look to the future with renewed energy, incentive and enthusiasm as we face even more challenging times ahead.

A handwritten signature in black ink, reading "Patrick B. Nixon". The signature is written in a cursive, flowing style with a large, prominent initial "P".

PATRICK B. NIXON
Director

Our Vision

Customers, Work Force, Partners → Raving Fans!

**Our vision focuses on people —
all working together to create “Raving Fans.”**



Who we are ...

From its headquarters at Fort Lee, Va., the Defense Commissary Agency operates a worldwide system of commissaries that provide quality grocery products at cost to active duty and retired military personnel, reservists, members of the National Guard, and their families.

Established by Congress more than 130 years ago, commissaries are considered an integral part of the military compensation package, providing the military community stationed throughout the world with significant savings on recognizable American products in a safe and secure environment.

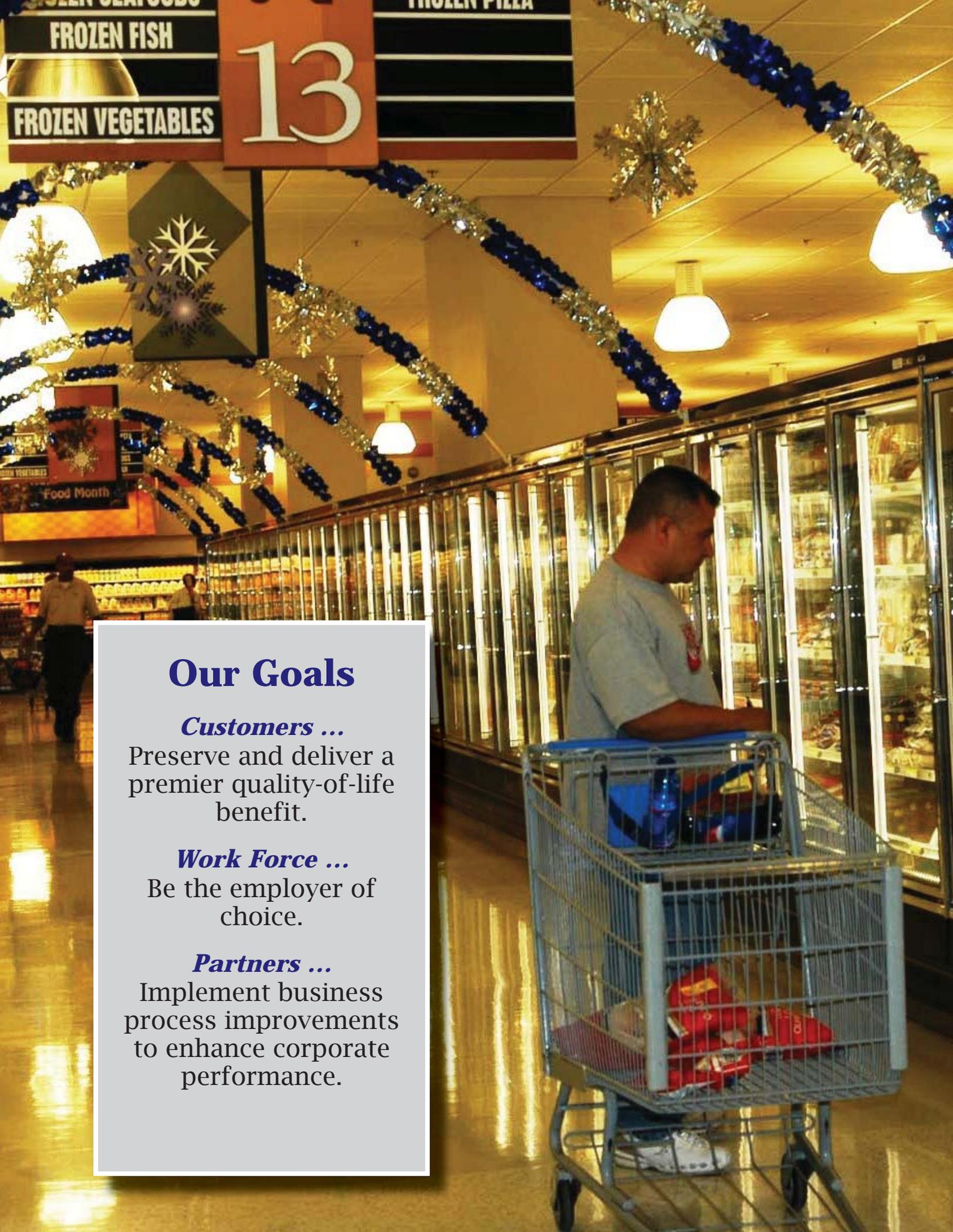
The Defense Commissary Agency was activated Oct. 1, 1991, consolidating duties and functions previously administered by the individual commissary systems of the four military services. The consolidation followed two years of planning that began in 1989 when the House Armed Services Committee directed the Defense Department to study the feasibility of consolidating the services' commissary systems to provide better service to military patrons at lower cost.

Today, three regional offices provide day-to-day management and support. Two of these operating elements, DeCA East and DeCA West, manage stores in the continental United States, Puerto Rico and the Pacific; one (DeCA Europe) manages commissaries in Europe. The agency also operates central distribution centers in Europe and the Pacific.

Field operating activities perform services for the regional offices and their commissaries that include centralized purchasing of national-brand sales items and centralized resale accounting.

The agency is managed in a cost-and-output culture where activity-based management is a way of life. This has enabled it to provide greater savings for service members and their families on the goods and services they purchase than at any other time in history — while at the same time holding down the cost to taxpayers.

A component of the Department of Defense, the agency reports to the undersecretary of defense for personnel and readiness. Oversight is provided by the Defense Department's Commissary Operating Board, comprised of senior officer, enlisted and civilian representatives from each of the military services and the secretariats of the military departments.



Our Goals

Customers ...

Preserve and deliver a premier quality-of-life benefit.

Work Force ...

Be the employer of choice.

Partners ...

Implement business process improvements to enhance corporate performance.

Who we serve ...

The Defense Commissary Agency delivers name-brand grocery products in a safe and secure environment and at exceptional savings to the men and women of the armed services community worldwide.

This premier quality-of-life benefit, consistently ranked by service members and their families as one of their top nonpay benefits, improves the financial viability of military families and other authorized patrons, aids in recruiting and retaining qualified people on active duty, helps maintain morale and fulfills prior commitments made to military retirees.

Commissary patrons purchase items at cost plus a 5-percent surcharge, which covers the cost of building new commissaries and modernizing existing ones. Shoppers save an average of more than 30 percent on their purchases compared to commercial prices — savings that exceed \$2,700 annually for a family of four that shops regularly at a commissary. These savings are particularly important for military families living overseas and in high-cost metropolitan areas of the United States.

Authorized users of the commissary benefit total about 12 million. These include all active and retired members of the uniformed services including the Coast Guard; members of the Reserve and National Guard; National Oceanic and Atmospheric Administration personnel; commissioned officers of the U.S. Public Health Service; the family members, widows and orphans of all such members; 100-percent-disabled veterans; Medal of Honor recipients; and Department of Defense civilian employees stationed overseas.



Our Values

“L I F E”

Leadership:

We expect passion, courage and excellence!

Integrity:

We demand honesty, professionalism and trustworthiness!

Flexibility:

We cultivate innovation, empowerment and competence!

Enjoyment:

We foster teamwork, recognition and opportunity!

What we accomplished ...

Fiscal 2005 was another impressive and successful year for the Defense Commissary Agency in terms of sales growth, customer service and fiscal responsibility.

► **Sales ...** During fiscal 2005, the agency posted annual sales \$5.369 billion, an increase of 2.5 percent — or \$133 million — over last year. This latest increase marked the third straight year of sales increases for the agency, setting another DeCA record.

Dept.	FY 2005 Sales	Change vs. FY04 Sales (%)	FY 2005 Savings (%)
Grocery	\$4,546,890,819	+ 2.1	27.5
Meat	\$ 440,733,202	+ 3.7	41.7
Produce	\$ 381,212,414	+ 6.5	33.4
Total	\$5,368,836,435	+ 2.5	32.0

Benchmark	DeCA	Industry Avg
Sales per sq foot/wk	\$ 15.25	\$ 7.47
Sales per checkout/wk	\$ 32,297	\$ 29,011

► **Unit cost ...** At the same time, costs came in under program. In fact, when measured in constant fiscal 2000 dollars, 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 customers — but because of efficiencies developed and deployed throughout the agency.

► **Customer service ...** In the areas of customer service and satisfaction, it was apparent commissary patrons liked what was happening, as evidenced by the overall customer service score of 4.55 (on a scale of 1 to 5) the agency received on its annual Commissary Customer Service Survey. These internal measurements were validated externally by the American Customer Satisfaction Index, which raised DeCA's fiscal 2005 score to 77 — three points higher than the national average for commercial supermarkets.

► **Fiscal responsibility ...** In addition to recording superior retailer-like statistics, DeCA also demonstrated it possesses the governance attributes of a model governmental entity, as evidenced by receiving a fourth consecutive clean audit opinion on its financial records. That audit looked at all of the agency's money accounts as well as its daily activities such as how accurately it records time and attendance and maintains physical inventory and accountability records.



“It is performance results like these that make it possible for us to set a self-imposed goal of increasing the value of the benefit without increasing its cost.”

— Patrick Nixon, DeCA director



Increasing the value of the benefit ...

Benchmarking visits with its business partners helped DeCA develop a number of initiatives aimed at increasing the value of the commissary benefit without increasing its cost.

▶ **“It’s Your Choice, Make It Healthy” ...** Partnering with TRICARE, the military’s health care provider, DeCA has developed “It’s Your Choice, Make It Healthy,” a program that highlights healthy foods available in military commissaries. Many larger commissaries have been configured with “Wellness Centers” to highlight these products for health-conscious patrons. In combination with this program, DeCA has increased the selection of natural and organic foods on its shelves.

▶ **Outsourcing produce ...** During fiscal 2005, DeCA tested a commercial-sector model to provide fresh fruit and vegetables for 20 of its commissaries. After test results validated this business concept as a more efficient business approach, DoD gave DeCA the OK to assume responsibility for contracting for its fresh fruit and vegetables. The first competitively awarded contract for 22 stores in the Mid-Atlantic area was completed in September 2005. By Sept. 30, 2006, DeCA expects to have contractors supplying all commissaries worldwide.

This new approach to acquiring produce supports DeCA’s goal to improve its efficiency and effectiveness in providing the commissary benefit and results in lower costs to DeCA, the federal government, produce suppliers and the patron.

▶ **Reshaping the work force ...** Early in 2004, DeCA developed a prototype store concept designed around a store work force that was simple, easy to manage, cost-effective and more productive. The final model eliminated 12 different position descriptions, replacing them with two — a multiskilled store associate and a general manager. The first two prototype stores — at Smokey Point, Wash., and Grand Forks Air Force Base, N.D. — have demonstrated the success of this concept.

▶ **Leveraging technology ...** To protect its customers from identity theft, DeCA integrated the best protection software and hardware that government and industry have to offer to deploy the most secure encryption system in military resale and one of the best in the retail world. Using the latest standards and technology, DeCA’s intrusion detection systems and firewalls protect and defend its systems against more than 2,000 attempts to crack into the network each month. As a result, DeCA earned the second highest score for data protection in DoD for 2005.

▶ **Outreach ...** Partnering with manufacturers and distributors, DeCA has extended its outreach efforts by bringing truckload sales of authorized commissary items to National Guard and Reserve centers.

Likewise, DeCA continues to assist its fellow resale organizations in delivering a “taste of home” to deployed forces in the Middle East. During fiscal 2005, the agency shipped over \$6 million in product to the Army and Air Force Exchange Service and the Navy Exchange Command from its distribution center in Europe to support military members in deployed areas.

“ ... we in DeCA are justifiably proud of the contributions we have made to the quality of life of our nation’s military and their families.” -- *Patrick Nixon, DeCA director*



Major challenges ...

Fiscal 2005 was also a year of challenges for the agency, marked by:

- Preparations for Base Realignment and Closure (BRAC) and re-stationing initiatives;
- Continued reorganization and centralization of support functions;
- Re-engineering of business processes to increase the value of the benefit without increasing its cost;
- Rising construction costs; and
- Hurricane damage and recovery

► **BRAC impact ...** The number of commissaries affected by installation closures under BRAC 2005 was not as great as anticipated. Only seven installations with commissaries are scheduled to close. However, resulting realignments due to closures and announced realignments will significantly affect the delivery of the commissary benefit. In many locations, stores will be too small to effectively handle the increased capacity. This presents a challenge for DeCA as it evaluates these needs and available funding alternatives. Completion of this task has been made more complex because overseas global re-stationing requirements have not been finalized.

► **Re-engineering ...** The purpose of DeCA's re-engineering efforts is to drive unnecessary costs out of the system so that it can reinvest those dollars to increase the value of the benefit to the patron. To that end, DeCA has focused its re-engineering efforts to optimize its business processes using Lean Six Sigma. The agency recently completed the first phase of six process-improvement projects that examined processes such as equipment inventory accountability and replacement, and commercial activity contracts.

► **Construction costs ...** One of DeCA's biggest challenges is the increase in construction costs. Over the last two years, many of the agency's projects have been impacted by the increased cost of building materials, fuel and utilities. In some cases, planned projects had to be deferred to have available sufficient funds to pay for others. In other cases, projects coming in at a cost more than what was expected had to be reduced in size.

Further, the requirement to incorporate force protection and antiterrorism standards in construction designs has had a negative impact on DeCA's surcharge account.

► **Hurricane damage and recovery ...** Like many other Americans, military families too suffered from the devastation inflicted upon the Gulf Coast by Hurricanes Rita and Katrina. When Katrina subsided, the Gulfport, Miss., store was unusable and the Keesler Air Force Base commissary was under water and had to be demolished; the New Orleans store fared better, suffering primarily product loss.

With the help of the military services, DeCA set up temporary facilities to provide the basic needs for military families as they returned to the storm-ravaged installations. The commissary at New Orleans reopened Sept. 29; repairs at Gulfport were scheduled to be completed in May 2006; but the Keesler store has to be entirely rebuilt.

Conclusion ...

The commissary benefit is critical to strengthening and preserving the armed services' quality of life and has an exceptionally positive impact on recruiting, retention and readiness of today's military.

The Defense Commissary Agency is committed to providing the armed services community with this valuable benefit to supplement military income as an integral part of the military's overall pay and benefits package.

In planning for the future, DeCA's strategies include expanding concepts and initiatives to increase the value of the benefit that took root in fiscal 2005. These include: "Virtual Commissary" — DeCA's entry into Internet sales of commissary items to its authorized patrons; CARTS — the Commissary Advanced Resale Transaction System — a major acquisition program to replace our stores' aging point-of-sale system; and eventual deployment of passive radio frequency identification technology.

As always, in all of its actions and initiatives, DeCA remains focused on its customers and we will continually strive to exceed their expectations while delivering both a critical economic advantage and a "taste of home" to service members deployed around the world.

We will remain the premier quality of life benefit to the men and women of the armed services community — relevant, responsive and recognized — a global mission serving a global force — the commissary benefit.

BRINGHOMETH
Savings

BRING HOME
THE
SAVINGS

DeCA
Financials

**DEFENSE COMMISSARY AGENCY
CONSOLIDATED BALANCE SHEETS
AS OF SEPTEMBER 30
(in thousands)**

	<u>2005</u>	<u>2004</u>
Assets		
Intragovernmental:		
Fund balance with Treasury (Note 2)	\$ 502,163	\$ 450,368
Accounts receivable and other	539	252
Total intragovernmental assets	<u>502,702</u>	<u>450,620</u>
Cash	99,198	96,318
Accounts receivable and other	61,079	51,387
Inventory	350,948	349,794
General property, plant, and equipment, net (Note 3)	804,914	825,787
Total assets	<u>\$ 1,818,841</u>	<u>\$ 1,773,906</u>
Liabilities (Note 4)		
Intragovernmental:		
Accounts payable	\$ 121,443	\$ 150,753
Other	39,898	39,976
Total intragovernmental liabilities	<u>161,341</u>	<u>190,729</u>
Accounts payable	447,293	401,990
Federal Employees Compensation Act actuarial liability	171,207	174,076
Environmental liabilities	31,866	9,015
Other	72,665	82,834
Total liabilities	<u>884,372</u>	<u>858,644</u>
Commitment and contingencies (Note 9)		
Net position (Note 5)		
Unexpended appropriations	50,384	17,816
Cumulative results of operations	884,085	897,446
Total net position	<u>934,469</u>	<u>915,262</u>
Total liabilities and net position	<u>\$ 1,818,841</u>	<u>\$ 1,773,906</u>

The accompanying notes are an integral part of the financial statements.

**DEFENSE COMMISSARY AGENCY
NOTES TO THE FINANCIAL STATEMENTS**

NOTE 2 - FUND BALANCE WITH TREASURY

FWBT consists of three types of funds – appropriated funds, revolving, and trust funds. Revolving funds involve DeCA’s Resale fund, trust funds involve the Surcharge fund, and appropriated funds include commissary operations, military construction, and procurement funds.

The following table shows the balance for each type of fund as of September 30, 2005 and 2004:

<u>Fund balances:</u>	<u>2005</u>	<u>2004</u>
Appropriated funds	\$ 233,476	\$ 193,962
Revolving funds	59,154	78,443
Trust funds	209,533	177,963
Total	<u>\$ 502,163</u>	<u>\$ 450,368</u>

The following table shows the status of the fund balances as of September 30, 2005 and 2004:

<u>Status of fund balances:</u>	<u>Appropriated</u>	<u>Revolving</u>	<u>Trust</u>	<u>Total</u>
Unobligated balance available	\$ 11,457	\$ -	\$ -	\$ 11,457
Unobligated balance unavailable	15	-	-	15
Obligated balance not yet disbursed, net of contract authority	222,004	59,154	209,533	490,691
Total as of September 30, 2005	<u>\$ 233,476</u>	<u>\$ 59,154</u>	<u>\$ 209,533</u>	<u>\$ 502,163</u>

<u>Status of fund balances:</u>	<u>Appropriated</u>	<u>Revolving</u>	<u>Trust</u>	<u>Total</u>
Unobligated balance available	\$ (27,140)	\$ -	\$ -	\$ (27,140)
Unobligated balance unavailable	43	-	-	43
Obligated balance not yet disbursed, net of contract authority	221,059	78,443	177,963	447,465
Total as of September 30, 2004	<u>\$ 193,962</u>	<u>\$ 78,443</u>	<u>\$ 177,963</u>	<u>\$ 420,368</u>

The unobligated available fund balance as of September 30, 2004 is negative because obligations exceed budget authority. Effective October 1, 1998, the Office of the Under Secretary of Defense (Comptroller) (OUSD(C)) established new Treasury codes, referred to as subheads, for the two activity groups within DeCA’s WCF. In conjunction with the establishment of the new Treasury codes, the OUSD(C) directed a transfer of net obligations, which were originally obligated under the old Treasury codes, to the Commissary Operations and Commissary Stock Resale activity groups. However, the OUSD(C) did not direct a transfer of the corresponding budget authority. In FY 2004, DeCA received a cash transfer from the Army, Navy, Air Force, and Defense-wide WCF accounts to DeCA’s WCF account in the amount of \$163.1 million to

**DEFENSE COMMISSARY AGENCY
NOTES TO THE FINANCIAL STATEMENTS**

help correct this underfunding. As of September 30, 2005, DeCA reports a positive \$11.4 million in unobligated balances available.

NOTE 3 - GENERAL PROPERTY, PLANT, AND EQUIPMENT

General property, plant, and equipment (PP&E) at September 30, 2005 and 2004 is summarized as follows:

<u>PP&E category</u>	<u>Acquisition</u> <u>Value</u>	<u>Accumulated</u> <u>Depreciation</u>	<u>Net</u>
Buildings, structures, and facilities	\$ 1,812,264	\$ (1,134,248)	\$ 678,016
Software	9,660	(5,555)	4,105
Equipment and other assets	175,318	(126,989)	48,329
Construction-in-progress	74,464	-	74,464
Total as of September 30, 2005	\$ 2,071,706	\$ (1,266,792)	\$ 804,914

<u>PP&E category</u>	<u>Acquisition</u> <u>Value</u>	<u>Accumulated</u> <u>Depreciation</u>	<u>Net</u>
Buildings, structures, and facilities	\$ 1,777,774	\$ (1,090,844)	\$ 686,930
Software	9,422	(4,540)	4,882
Equipment and other assets	177,914	(112,363)	65,551
Construction-in-progress	68,424	-	68,424
Total as of September 30, 2004	\$ 2,033,534	\$ (1,207,747)	\$ 825,787

**DEFENSE COMMISSARY AGENCY
NOTES TO THE FINANCIAL STATEMENTS**

NOTE 4 - LIABILITIES

The following table summarizes total liabilities covered and not covered by budgetary resources as of September 30, 2005 and 2004:

	<u>Covered by Budgetary Resources</u>	<u>Not Covered by Budgetary Resources</u>	<u>Total</u>
<u>Intragovernmental:</u>			
Accounts payable	\$ 121,443	\$ -	\$ 121,443
Other	2,722	37,176	39,898
Subtotal	124,165	37,176	161,341
<u>With the public:</u>			
Accounts payable	447,293	-	447,293
Federal Employees Compensation Act actuarial liability	-	171,207	171,207
Environmental liabilities	-	31,866	31,866
Other	22,260	50,405	72,665
Subtotal	469,553	253,478	723,031
Total as of September 30, 2005	\$ 593,718	\$ 290,654	\$ 884,372

	<u>Covered by Budgetary Resources</u>	<u>Not Covered by Budgetary Resources</u>	<u>Total</u>
<u>Intragovernmental:</u>			
Accounts payable	\$ 150,753	\$ -	\$ 150,753
Other	2,385	37,591	39,976
Subtotal	153,138	37,591	190,729
<u>With the public:</u>			
Accounts payable	401,990	-	401,990
Federal Employees Compensation Act actuarial liability	-	174,076	174,076
Environmental liabilities	-	9,015	9,015
Other	33,018	49,816	82,834
Subtotal	435,008	232,907	667,915
Total as of September 30, 2004	\$ 588,146	\$ 270,498	\$ 858,644

**DEFENSE COMMISSARY AGENCY
NOTES TO THE FINANCIAL STATEMENTS**

Other liabilities consist primarily of workers' compensation, accrued payroll and benefits, accrued unfunded annual and other leave, and foreign national separation pay. The following table summarizes other liabilities current and non-current as of September 30, 2005 and 2004.

<u>Other liabilities</u>	<u>Current</u>	<u>Non-Current</u>	<u>Total</u>
<u>Intragovernment:</u>	<u>Liabilities</u>	<u>Liabilities</u>	
Workers compensation	\$ 15,938	\$ 21,238	\$ 37,176
Employer contributions and payroll taxes payable	2,722	-	2,722
Subtotal	<u>18,660</u>	<u>21,238</u>	<u>39,898</u>
 With the public:			
Accrued funded payroll and benefits	22,260	-	22,260
Foreign national separation pay	12,336	-	12,336
Accrued unfunded annual leave	38,069	-	38,069
Subtotal	<u>72,665</u>	<u>-</u>	<u>72,665</u>
Total as of September 30, 2005	<u>\$ 91,325</u>	<u>\$ 21,238</u>	<u>\$ 112,563</u>

<u>Other liabilities</u>	<u>Current</u>	<u>Non-Current</u>	<u>Total</u>
<u>Intragovernment:</u>	<u>Liabilities</u>	<u>Liabilities</u>	
Workers compensation	\$ 16,696	\$ 20,832	\$ 37,528
Employer contributions and payroll taxes payable	2,385	-	2,385
Other	63	-	63
Subtotal	<u>19,144</u>	<u>20,832</u>	<u>39,976</u>
 With the public:			
Accrued funded payroll and benefits	38,572	-	38,572
Foreign national separation pay	11,669	-	11,669
Accrued unfunded annual leave	38,147	-	38,147
Liability for deposit funds	(5,554)	-	(5,554)
Subtotal	<u>82,834</u>	<u>-</u>	<u>82,834</u>
Total as of September 30, 2004	<u>\$ 101,978</u>	<u>\$ 20,832</u>	<u>\$ 122,810</u>

**DEFENSE COMMISSARY AGENCY
NOTES TO THE FINANCIAL STATEMENTS**

NOTE 5 - NET POSITION

The following table summarizes the net position by fund type as of September 30, 2005 and 2004:

<u>Net position:</u>	<u>General</u> <u>Fund</u>	<u>Working</u> <u>Capital</u> <u>Fund</u>	<u>Total</u>
Unexpended appropriations	\$ 598	\$ 49,786	\$ 50,384
Cumulative results of operations	949,289	(65,204)	884,085
Total as of September 30, 2005	\$ 949,887	\$ (15,418)	\$ 934,469

<u>Net position:</u>	<u>General</u> <u>Fund</u>	<u>Working</u> <u>Capital</u> <u>Fund</u>	<u>Total</u>
Unexpended appropriations	\$ 345	\$ 17,471	\$ 17,816
Cumulative results of operations	950,018	(52,572)	897,446
Total as of September 30, 2004	\$ 950,363	\$ (35,101)	\$ 915,262

NOTE 9 - CONTINGENCIES

DeCA is a party in various administrative proceedings, legal actions and tort claims which may ultimately result in settlements or decisions adverse to the Federal government. DeCA has not accrued any amounts for contingent liabilities as the potential losses have not been determined to be probable and/or the amounts cannot be estimated. The amounts claimed related to the significant cases total approximately \$1.3 million as of September 30, 2005.

