DOD BASE LODGING: THE CASE FOR PRIVATIZATION

The Military Housing Privatization Initiative (MHPI) authorities (10 USC §§ 2871, et seq.) have transformed once-dilapidated military family housing into thriving communities by allowing private sector capital to redevelop on-base facilities and improve the quality of life for Service Members and their Families. Given privatization's success, the Army expanded its use of the MHPI authorities in the United States through its Privatization of Army Lodging (PAL) program. The Army's lodging facilities had deteriorated over the years due to the cumulative impact of deferred maintenance and a lack of strategic reinvestment. While the Army had a need for on-base lodging, it had no need to be in the hotel business. Privatization was deemed a proven path for raising the necessary private capital, implementing best business practices, reducing government manpower and maintenance costs, and exiting a noncore function. Privatization would also ensure the long-term sustainment of the facilities in support of the mission.

The Army has privatized 13,602 on-base guestrooms across 40 installations and the PAL Project Company has met or exceeded expectations with regard to development, operations, and financial performance. Work has been completed on-time and on-budget budget, demand has been strong, guest and garrison satisfaction scores have been excellent, and net operating income has been in-line with pro forma expectations. The Army has shown that privatization can provide quality, cost-effective accommodations while offering government savings and cost-avoidances in a time of reduced federal funding. In brief, the benefits of expanding the Army's privatized lodging program across the DoD include:

Divesting a Noncore Function: As part of then-President Bush's Presidential Management Agenda, the Services were charged with reviewing and eliminating noncore functions. In endorsing the privatization of lodging, then-SECARMY Harvey specifically cited this noncore determination. Of all the potential courses of action being evaluated by the Office of the Deputy Chief Management Officer (DCMO) for base lodging, it is privatization alone that both saves significant travel dollars and conforms with the requirements of the Office of Management and Budget's (OMB) Memorandum M-17-22, "Comprehensive Plan for Reforming the Federal Government and Reducing the Federal Civilian Workforce" to exit nonessential functions.

Reducing DoD Manpower Costs: The PAL program eliminated 2,379 DoD positions (80% of Army Lodging staff) and transitioned the vast majority of them to private-sector employment. All told, 89% of the available positions were filled with former Army Lodging employees. The PAL hotelier offers competitive wage and benefit packages to its employees and, while it was once viewed with trepidation, former Army Lodging employees have lauded the transition. Privatizing the remaining DoD domestic on-base lodging operations would transition nearly 7,500 employees from federal to private employment. Additional manpower reductions would be possible were the DoD to direct the privatization of overseas lodging through existing authorities in lieu of extending the reach of the MHPI statute through legislative amendment. Unlike DoD Lodging, Army oversight of the PAL project requires only five government full-time equivalents.

Military Service	Employees Federal ⇨ Private
Army	2,379 ✓
Air Force	3,851
Navy	3,465
Marines	163

Discounted Rates: Under the PAL program, the Army has capped official traveler costs at a weighted average of 75% of the lodging per diem across the portfolio. This low 75% of per diem rate is sufficient to cover all operational expenses including those that had once been paid by installation APF subsidies. The rate ($75.16 in FY16) also funds all recapitalization and sustainment requirements. The 25% official traveler discount at the privatized hotels represents an annual cost avoidance of $83M compared to full per diem.

Installation Savings: The low rates previously charged by Army Lodging were an illusion. There were significant, fixed appropriated fund (APF) costs borne at every installation to support the non-appropriated fund (NAF) Army Lodging operation. These costs included all utility expenses, a significant amount of maintenance and repair work performed by the Department of Public Works, non-NAF employees supporting the operation, numerous support contracts (laundry, telecommunications, pest control, landscaping, etc.) and municipal services. The lack of transparency into these APF costs made it difficult for the Army to understand and efficiently manage its all-in lodging expenses. Under privatization, there are no longer any hidden costs as direct APF support is eliminated in its entirety and the room rates represent the true and only cost of official on-base lodging.

Recapitalization: A 2003 independent A&E study found that 80% of the Army Lodging inventory did not meet basic DoD standards (including some life-safety requirements) with more than a billion dollars in new construction and renovation required (twice the initial, internal Army Lodging estimate). Army Lodging's plan to address recapitalization through a nightly surcharge was deemed inadequate by the Army because it would take decades to build out the requirement and did not offer an adequate long-term sustainment component. By contrast, as of mid-FY17, the PAL partner has completed more than half a billion dollars in new construction and renovation and branded 41% of the end-state rooms.

Before & After Privatization – Yuma Proving Ground, AZ

Long-Term Sustainment: The use of revenue collected by the PAL Project Company is governed by the lease and other Army-approved legal agreements. Of every $100 dollars earned, $43 goes into a lockbox used exclusively for Army-approved new construction, renovation, and long-term sustainment requirements – there is no PAL Project Company "profit," there is only a PAL reinvestment account.

Meeting the Mission: Eight years into privatization, the PAL partner has accommodated trainees, military families, wounded warriors, distinguished visitors, flight crews, business travelers, emergency relief workers, foreign students, contractors, retirees – anyone and everyone that has needed to stay on-base in support of the mission. Feedback on privatization from Garrison Commanders and guests alike has been overwhelmingly positive and government interests have been protected through Army-approvals embedded in the lease or addressed though the Army's asset management program.

Proven Results: Occupancy and financial performance have been strong. Ribbon-cutting ceremonies for on-base Holiday Inn Express hotels and new Candlewood Suites hotels are occurring with increasing regularity as official travelers enjoy enhanced service offerings, new amenities and frequent-stay points. Relative to the government, operating expenses and construction costs are far less, allowing the private sector to generate additional recapitalization funds and stretch those dollars further. The Army's privatized lodging program is no longer a speculative venture. It has delivered on its promise and done so with no government equity and no government financial or occupancy guarantees of any kind. The business case for privatized lodging is in evidence every day across the Army. No additional studies are required. There is no material difference between the on-base lodging facilities at an Air Force, Navy, or Marine Corps base today and those that were privatized nearly a decade ago by the Army.

Immediate Savings: One of the immediate benefits of implementing lodging privatization is that the existing government lodging operations can immediately discontinue collecting most recapitalization funds through their room rates since there will not be enough time (or a need) to execute those funds. The multi-billion-dollar recapitalization requirement will shift to the private sector post-privatization at rates set by the DoD to preserve cost savings, cover operating expenses, and recapitalize the inventory. During the three- to four-year private partner acquisition process, rates paid by the DoD will drop by approximately $100M per annum delivering up to ***$400M in cost avoidance in the next few years*** – precisely the timeframe when the DoD is searching for scarce dollars to increase the lethality of the force.

Lodging privatization offered the Army a means to recapitalize and sustain its on-base lodging inventory while locking-in low room rates. As budget cuts drive the need for change and innovation, it is not a time for incremental change or oft-promised and rarely-realized government consolidation "efficiencies." The other Services have an opportunity to take advantage of the Army's lessons learned, template documents, and in-house expertise to efficiently and effectively transition to privatized base lodging and create a single DoD enterprise standard. To accomplish this, the SECDEF must direct the Services to take action. Once green-lit, the requisite due diligence, real estate/environmental work and stakeholder engagement can be completed. Given that the Office of the ASD for Energy, Installations, & Environment has principal responsibility for all matters pertaining to lodging privatization efforts under DoD Manual Number 4165.63-M, it should have a larger role in the lodging reform initiative going forward. By leveraging the experienced team and stable platform offered by the existing MHPI & PAL programs, the other Services could divest of this noncore function and privatize the entirety of their on-base lodging operations no later than 2021.

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