DEFENSE-WIDE WORKING CAPITAL FUND
DEFENSE LOGISTICS AGENCY
FISCAL YEARS (FY) 2000/2001 BIENNIAL BUDGET ESTIMATE
DISTRIBUTION DEPOTS

FUNCTIONAL DESCRIPTION

The Defense Logistics Agency (DLA) Distribution Depots Activity Group is responsible for the receipt, storage, and issue of approximately 21 million lines of workload. During FY 1998, DLA began realigning the DLA distribution depot system, which consisted of two Distribution Regions located at New Cumberland, PA (DDRE) and Stockton, CA (DDRW), into one command -- the Defense Distribution Center (DDC) at New Cumberland, PA. Each of the current 21 distribution depots reports to the DDC. Customers include components of all Military Services, defense agencies and authorized civil agencies within designated geographical areas.

The realignment is part of an overall reduction of Department of Defense (DoD) support activities and will allow DLA to bring its operating costs into line with today's smaller military force. By eliminating one of two existing regions and streamlining the remaining management structure, DLA will eventually need about 850 fewer people. During FY 1998, we achieved a reduction of 355 personnel and have estimated savings at $16 million in FY 1999, a year earlier than expected. Beginning in FY 2000, we estimate achieving total savings of $34 million per year and a total of 850 people.

In 1998, DLA began the process of competing the first 3 of 16 depots with private industry. Planned for competition are an additional 7 depots in FY 1999 and 6 depots in FY 2000. DLA's 2 primary distribution depots at Susquehanna, PA and San Joaquin, CA are also planned for review. Based on the results of the first round of Distribution's A-76 competition, DLA will review all activities at these two sites deemed not to be inherently governmental. One of the Base Realignment and Closure(BRAC)distribution depots, San Antonio, TX, was directly converted to contractor operations in March 1998. Under the A-76 competition process, it is anticipated that depot labor will be reduced 20 percent by establishing the most efficient organization. One half of all depot competitions are assumed to be awarded to private contractors. Savings are assumed for all competitions. The typical competition will take 24 months from time of announcement to contract award.

Estimated costs/assumptions for the competitions are as follows:

(1) Study costs estimated at $2,000 per full-time equivalent (FTE);
(2) Severance costs for personnel reductions and contract conversions for half of the depots being studied estimated at $28,000 per FTE;
(3) Assumed that 80 percent of personnel reductions would require severance costs; and
(4) For those depots assumed to be contracted out, a quality assurance evaluation cost was included and was estimated at 3 percent of the post-most efficient organization (MEO) workforce.

The FTE billet and labor savings reported only include MEO savings. A one-time savings of 3 percent of the Inter-Service Support Agreement costs was assumed at contracted depots. Costs and savings were prorated by month to the fiscal year in which they are expected to occur. DLA estimates the completion of the entire competitive process by the end of FY 2001.

The Distribution portion of the Materiel Management Business Plan is currently being revised to reflect the ever-changing business environment. The existing plan consists of nine goals specific to Distribution:

(1) Dramatically improve response time, reliability, and communications;
(2) Greatly reduce the total cost to our customers;
(3) Invest in our people to enable them to deliver and sustain world class logistics performance levels;
(4) Significantly enhance the ease with which we interface and partner with our suppliers;
(5) Reduce the infrastructure needed to accomplish our mission;
(6) Integrate logistics research and development into the planning and delivery of future integrated logistics capabilities;
(7) Significantly expand our use of commercial business practices in the execution of our mission;

(8) Develop and execute an overall strategy for leveraging information technology into our integrated logistics solutions; and
(9) Create a seamless logistics support process that moves materiel from the factory to the customer rapidly and with minimal intermediate handling.

The primary focus of these efforts is to reduce logistics cycle times and to streamline the infrastructure. In addition, we are moving to a much more agile and responsive Distribution system. Our processing time frames have been dramatically reduced in an effort to help the Services and DLA achieve the various Streamlining Logistics efforts ongoing DoD-wide.

DLA has been able to make great steps in reducing the number of depots, through BRAC Commission decisions in 1993 and 1995, from 30 depots in 1992 to 21 in 1999. Ogden, UT and Memphis, TN depots closed and Columbus, OH depot realigned in FY 1997. The Letterkenny, PA depot closed in FY 1998. A residual workforce will remain at Letterkenney as a satellite operation of the Defense Distribution Susquehanna, PA. The San Antonio, TX distribution depot operations were outsourced March 1998. The contractor will redistribute remaining materiel to other DLA storage locations as directed, with closure under BRAC scheduled for July 2001. The last BRAC distribution depot scheduled for closure is McClellan, in Sacramento, CA. Workforce reductions began in FY 1998 and will continue through FY 2000. Closure date is July 2001. These closures should result in significant future savings and will be passed on to customers and are reflected in this budget.

Navy and DLA have agreed that DLA will assume the Distribution function currently performed by Navy at Pearl Harbor, Hawaii and Yokosuka, Japan. The distribution functions are portions of the current Navy Fleet Industrial Support Center operations at these sites. This will allow Navy to avoid costs related to maintenance of a unique automated warehousing system, lower Navy's infrastructure and cost, improve material flow, and offer benefits of standardization and warehousing expertise. Transfer is to become effective April 1, 1999, on a reimbursable basis. There will be 21 depots remaining after BRAC-designated depots have been closed and the acquisition of these two Navy depots.

To date, overall performance has improved while costs continue to decrease. Continuing process efficiencies and a steady drop in mission workload have led to significant reductions in the Distribution workforce. Endstrength dropped from 27,000 in FY 1992 to 11,357 in FY 1998, a reduction of 15,643 personnel, or a 57.9 percent decrease. Additional reductions of 1,074 endstrength by the end of FY 2000 are reflected in this budget. Reductions to date have been accomplished mainly through the use of the Voluntary Separation Incentive Pay (VSIP) and Voluntary Early Retirement Authority (VERA). However, involuntary Reductions-in-Force (RIFs) were required in FY 1998, and more may be required in FY 1999, to maintain the appropriate balance of workforce to workload.

Distribution's Performance and Quality Measures are shown below:

Performance Measure	Goal	FY 1998 Actual	FY 1999 Estimate	FY 2000 Estimate
High Priority Material Release Orders (MROs)	1.0 day	0.6	1.0	1.0
Routine MROs	1.0 day	1.0	1.0	1.0
Sample Inventory Accuracy	95%		95%	95%
Distribution Standard System (DSS)		81%		
Navy Statman		93%		

PERSONNEL PROFILE:

	FY 1998	FY 1999	FY 2000
Civilian End Strength	11,357	11,358	10,283
Civilian Full Time Equivalents (FTEs)	12,346	11,721	10,651
Military End Strength	139	142	142
Military Workyears	139	142	142

BUDGET HIGHLIGHTS:

WORKLOAD:

Lines Received and Shipped:

Line items either received or shipped is the basic work count. Lines received and shipped workload declined 5.5 percent from FY 1997 to FY 1998. Workload is budgeted to decline an additional 15.7 percent through FY 2000. Reengineering initiatives such as Premium Service, Virtual Prime Vendor and Central Depot concept, along with a general decline in customer demands, will continue this trend into the foreseeable future. These estimates reflect the latest forecasts.

Lines Received and Shipped (Millions)

FY 1998	FY 1999	FY 2000
25.9	23.4	21.6

Storage:

In FY 1996, Discrete Pricing was implemented to allow, for the first time, the separate recovery of the cost to store DoD materiel. This initiative charges inventory owners for the storage of materiel based on square footage occupied in warehouses. In FY 1999, we changed from gross square feet occupied to cubic feet of warehouse space occupied. This change better reflects the real cost of storage, since all bin and rack storage, plus a large percentage of bulk space, have storage aids that take advantage of the full stacking height of our warehouses. This change takes into account benefits derived from modern high rise/low cost per cubic foot storage practices. It mirrors commercial practice. It also includes the appropriate billing for commingled stock. Our storage rate remains relatively stable in lieu of decreasing because of declining demand and the challenge of reducing fixed costs in the short-term. Occupied cubic feet of storage declined 15 percent from FY 1997 to FY 1998. Occupied cubic feet of storage is budgeted to decline an additional 18 percent through FY 2000.

Average Cubic Footage Occupied (Millions)

	FY 1998*	FY 1999	FY 2000
Covered Storage Space	34.8	291.8	283.0
Open Storage Space	14.3	78.6	76.9

* Space and rate calculated in square feet in FY 1998. Changed from square feet to cubic feet in FY 1999.

REVENUE:

Revenue for the Distribution Depots Activity Group consists of payments from the DLA and Services'Supply Management Activity Groups for lines received and shipped, for storage space occupied, and reimbursable funding provided by inventory managers or local activities to depots for special project work. Inventory Control Points (ICPs) in supply management include their distribution depot costs in surcharges applied to sales of materiel that they manage.

The discrete pricing structure includes a matrix of discrete prices for lines received and shipped, a separate pricing structure for storage services and an hourly reimbursable rate.

Lines Received and Shipped:

Inventory Control Points reimburse Distribution for lines received and shipped charges based on a discrete pricing structure matrix.

Lines Received and Shipped:	FY 1998	FY 1999	FY 2000
Receipts			
Bin	$ 25.53	$28.72	$24.55
Medium Bulk	27.81	40.11	38.59
Heavy Bulk/Hazardous	39.31	53.85	63.29
Issues On-Base:			
Bin	11.36	16.07	13.95
Medium Bulk	20.29	32.64	31.10
Heavy Bulk/Hazardous	46.14	63.16	57.34
Issues Off-Base:			
Bin	14.91	16.96	17.18
Medium Bulk	31.31	43.16	38.49
Heavy Bulk/Hazardous	68.46	81.71	88.88
Transshipments	2.07	3.22	5.25
Composite Rate	$22.09	$27.97	$26.34
Percentage Change	+19.5%	+26.6%	-5.8%

Processing rates were under-priced in FY 1998, primarily as a result of higher workload decline than expected. We increased rates in FY 1999 to offset prior year losses. Having done so, we were able to reduce our rates in FY 2000 and still recover total costs.

Storage:

Storage charges were initially included as part of the DLA FY 1996 Discrete Pricing initiative. The separate recovery of cost to store DoD materiel is identified and charged to the inventory owners. In FY 1999, we changed the unit rate from gross square feet occupied to cubic feet of warehouse space occupied in order to better reflect the actual cost of storage and to give our customers visibility of their occupied space and associated costs. We have seen overall occupied storage decline significantly as our customers experienced, and reacted to, the cost to hold inventory.

Our overall negligible rate increase (an additional $.02 for open storage) demonstrates the change in behavior we hoped our discrete prices would drive. A rate adjustment is necessary to ensure our revenue covers our costs as we attempt to shed infrastructure.

Average Cost per Cubic Foot

	FY 1998*	FY 1999	FY 2000
Covered Storage	$7.89	$.83	$.83
Open Storage	$0.85	$.15	$.17

* Space and rate calculated in square feet in FY 1998. Changed from square feet to cubic feet in FY 1999.

Capital Investments:

The Capital Investment Program for Distribution is for the reinvestment of the infrastructure for this activity group. The Distribution Activity group submits the following requirements:

($000)	FY 1998	FY 1999	FY 2000
Equipment (non-ADP)	20,961	20,021	18,687
Equipment (ADP/T)	13,948	5,604	5,652
Software Development	15,427	7,773	9,279
Minor Construction	7,666	6,900	5,100
TOTAL	58,002	40,298	40,548

The decrease in software development reflects the successful completion of the Distribution Standard System (DSS) operating system.

Operating Result: Distribution suffered a negative net operating result in FY 1998. Factors contributing to this loss are the execution of stabilized rates to a larger than projected decrease in lines received and shipped workload, and an over-estimated hourly reimbursable workload.

Net Operating Result (NOR)/Accumulated Operating Result (AOR)

(Dollars in Millions)

	FY 1998	FY 1999	FY 2000
NOR	-57.9	91.8	1.0
Prior Year AOR	-47.2	-105.1	-13.3
AOR	-105.1	-13.3	-12.3

Pursuant to the current policy of total cost recovery within two budget years, workload and prices have been adjusted in FY 1999 and FY 2000 to achieve total cost recovery by FY 2001.

Activity Group Operations Fund Defense Logistics Agency Distribution Depots Revenue and Expenses (Dollars in Millions)			
	FY 98	FY 99	FY 00
Revenue:			
Gross Sales	0.0	0.0	0.0
Operations	1,376.5	1,511.6	1,331.4
Capital Surcharge	0.0	0.0	0.0
Depreciation excluding Maj Const	18.9	32.9	57.1
Major Construction Dep	0.0	0.0	0.0
Other Income			
Total Income:	1,395.4	1,544.5	1,388.5
Expenses:			
Cost of Material Sold from Inventory	0.0	0.0	0.0
Salaries and Wages:			
Military Personnel	11.4	8.8	9.2
Civilian Personnel	581.5	583.1	543.4
Travel & Transportation of Personnel	5.5	5.0	4.9
Materials & Supplies (for Internal Operations)	23.9	23.6	24.1
Equipment	0.0	0.0	0.0
Other Purchased Services from Revolving Funds	78.6	85.7	85.6
Transportation of Things	468.4	448.7	400.1
Depreciation-Capital	18.9	32.9	57.1
Printing and Reproduction	1.6	1.7	1.7
Advisory and Assistance Services	0.0	0.0	0.0
Rent, Communication, Utilities, & Misc. Charges	11.0	10.9	11.2
Other Purchased Services	252.5	252.3	250.2
Total Expenses	1,453.3	1,452.7	1,387.5
Operating Result	(57.9)	91.8	1.0
Less Capital Surcharge Reservation	0.0	0.0	0.0
Plus Appropriations Affecting NOR/AOR	0.0	0.0	0.0
Other Changes Affecting NOR/AOR	0.0	0.0	0.0
Net Operating Result	(57.9)	91.8	1.0
Prior Year AOR	(47.2)	(105.1)	(13.3)
Accumulated Operating Result	(105.1)	(13.3)	(12.3)
Non-Recoverable Adjustment Impacting AOR	0.0	0.0	0.0
Accumulated Operating Results for Budget Purposes	(105.1)	(13.3)	(12.3)

Activity Group Analysis
Defense Logistics Agency
Distribution Depots
Source of New Orders and Revenue
(Dollars in Millions)

	FY 98	FY 99	FY 00
1. New Orders			
a. Orders from DoD Components:	83.7	107.5	77.2
Other Services (Appropriated)			
DLA	18.6	53.0	36.9
Army	37.6	38.4	34.2
Navy	0.0	0.0	0.0
Air Force	11.2	16.1	6.1
Marine Corps	0.0	0.0	0.0
Defense Environmental Restoration Act	6.2	0.0	0.0
National Imagery and Mapping Agency	10.1	0.0	0.0
b. Orders from Other Working Capital Fund Activity Groups:	1,311.7	1,437.0	1,311.3
DLA	716.0	775.2	670.4
Army	241.6	216.9	225.5
Navy	131.4	169.2	177.2
Air Force	211.6	266.7	229.6
Marine Corps	11.1	9.0	8.6
c. Total DoD:	1,395.4	1,544.5	1,388.5
d. Other Orders:	0.0	0.0	0.0
Other Federal Agencies			
Trust Fund			
Non Federal Agencies			
Foreign Military Sales			
2. Carry-In Orders	0.0	0.0	0.0
3. Total Gross Orders	1,395.4	1,544.5	1,388.5
4. Funded Carry-over	0.0	0.0	0.0
5. Total Gross Sales	1,395.4	1,544.5	1,388.5

Exhibit Fund-11 Source of New Orders & Revenue

Changes in the Costs of Operations
Defense Logistics Agency
Distribution Depots
(Dollars in Millions)

		EXPENSES	
FY 1998 Estimated Actual		1,475.3	
FY 1998 Actual		1,453.3	
Impact in FY 1998 of Actual FY 1998 Experience:			
Depreciation		(30.1)	
Personnel Costs		(90.7)	
Travel & Transportation of Personnel		(1.8)	
Materials & Supplies (For Internal Operations)		(2.0)	
Equipment		(13.7)	
Transportation		61.1	
Printing & Reproduction		(0.2)	
Rent, Communication, Utilities, & Misc. Charges		(4.3)	
Other Purchased Services		59.7	
Pricing Adjustments:			
Annualization of FY 1998 Pay Raise		4.0	
FY 1999 Pay Raise		15.1	
Purchase Inflation		13.4	
Program Changes:			
A-76 Competitions		4.0	
Base Realignment and Closure		(19.6)	
Corporate Overhead Allocation		(18.2)	
Corporate Restructuring		(16.0)	
Defense Environmental Restoration Act		(13.4)	
Depreciation		9.5	
Defense Finance and Accounting Service		(1.0)	
Military Personnel		(3.1)	
National Imagery and Mapping Agency		9.3	
Real Property Maintenance		15.4	
Workload Decrease		(22.9)	
Year 2000 Testing		3.8	
Pearl Harbor & Yokosuka Depots Transfer Reimbursement		19.1	
FY 1999 Current Estimate		1,452.7	

Exhibit Fund-2 Changes in the Costs of Operation

Changes in the Costs of Operations
Defense Logistics Agency
Distribution Depots
(Dollars in Millions)

		EXPENSES	
FY 1999 Current Estimate		1,452.7	
Pricing Adjustments:			
Annualization of FY 1999 Pay Raise		5.0	
FY 2000 Civilian Personnel Pay Raise		19.5	
FY 2000 Military Personnel Pay Raise		0.2	
Fuel Inflation		0.1	
Purchase Inflation		11.8	
Program Changes:			
A-76 Competitions		7.5	
Base Realignment and Closure		(30.8)	
Corporate Overhead Allocation		7.2	
Corporate Restructuring		(34.0)	
Depreciation		21.2	
Defense Finance and Accounting Service		6.3	
Over Ocean Transportation		(29.6)	
Real Property Maintenance		1.9	
Workload Decrease		(67.5)	
Pearl Harbor & Yokosuka Depots Transfer		19.1	
Military Personnel		0.7	
Year 2000 Testing		(3.8)	
FY 2000 Estimate		1,387.5	