WORKING CAPITAL FUNDS AND TWO-TIER PRICING

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WORKING CAPITAL FUNDS 101

WHAT IS A WORKING CAPITAL FUND?

- An account at the US Treasury through which the operations of one or more activities (organizations) are funded
- DOD has five WCF
  - 3 for Military Department activities
  - 1 for Defense-wide activities
  - 1 for the Defense Commissary Agency
  - Plus several revolving funds

WHAT TYPES OF ACTIVITIES DO WCF FUND?

- Supply
- Depot maintenance
- Transportation
- Communications
- Information processing
- Finance and accounting
- Printing and publication
- Personnel security investigations
- Commissaries
- R&D and public works (DON only)

HOW DO WCF ACTIVITIES OPERATE?--1

- Like a business
  - Acquire, capitalize and depreciate assets
  - Get orders from customers
  - Do work or sell goods
  - Pay employees and vendors
  - Bill customers, collect some payments, and have bad debts
  - Maintain working cash and take out short term loans by billing in advance
  - Make a profit or loss in any particular year

HOW DO WCF ACTIVITIES OPERATE?--2

- Like a regulated utility
  - Have a monopoly in some cases
  - Must meet needs of all customers
- Like a not-for-profit
  - Try to break even
- Unlike a business
  - Mission support is paramount
  - Charge rates set in advance (stabilized rates)
  - Maintain “mobilization” capabilities
  - Operate under restrictions that do not apply to private sector entities

BENEFITS

- Greater efficiency through pressures of market on buyers and sellers
- Protection of readiness through stabilized rates
  - Ensure adequate funding for expected activity level
  - Fund can absorb losses in the short run
- Cost visibility
- Some greater flexibility in use of funds

WCF AND THE PRIVATE SECTOR

- WCF have a monopoly by law or policy
  - And do most work in house
  - But use extensive out sourcing
  - Monopoly only extends to a portion of work
- WCF have a de facto monopoly in short run
- WCF have won public-private competitions
- No private sector entity has bid
- Customers have freedom to choose

SETTING PRICES (RATES)

- Break even on an accrual basis
  - Covering all costs except mobilization costs
- Ensure adequate cash
- Recover unanticipated losses or return unanticipated profits from prior years

PROBLEMS IN SETTING RATES

- Customers do not know their full costs
- Allocating overhead
- Recovering mobilization costs
  - Policy is to exclude them from rates
  - Not always done
  - Major examples
    - Marginal cost of moving cargo on military training flights
    - DISA's mobilization costs

COVERING DISN MOBILIAZTION COSTS

TWO-TIER PRICING

WHAT ARE MOBILIZATION DISN CAPABILITIES?

- Excess capacity
- Military-unique features
- Cost to get into the long-haul system

THE PROBLEM

- DISA was including all costs in rates, making rates higher that those charged by the private sector
- Customers were buying directly from the private sector vice using DISN
- Total costs to DOD was higher than necessary

THE SOLUTION

- Charge customers rates at (or below) commercial rates (Tier 2 costs)
- Divide remaining costs (Tier 1) among Services and Agencies to be paid at the corporate level (Service Level Bill)
- Implemented in the FY00 budget
- Eliminated the cost incentive to most customers to buy directly

IMPLEMENTATION

- Problems
  - Determining commercial rates
  - Relating remaining costs to mobilization costs
  - Allocating Tier 1 costs
- Evidence of success
- Remaining issues