

PRIVATIZED ARMY LODGING (PAL): 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 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-post 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, and significantly reducing government manpower and maintenance costs. Privatization would also ensure the long-term sustainment of the facilities in support of the mission.

To date, the Army has privatized more than 11,600 on-post guestrooms across 39 installations. The PAL Project Company has met or exceeded expectations with regard to development, operations and financial performance. Work has been completed ahead of schedule and under 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 the government savings and cost-avoidances in a time of reduced federal funding. In brief, the benefits of privatized on-post lodging include:

Recapitalization: A 2003 independent A&E study found that 80% of the lodging inventory did not meet basic Army Lodging standards (including some FEMA life-safety requirements) with \$1.1B in new construction and renovation required (twice the internal Army Lodging estimate). Army Lodging's plan to address the recapitalization, a \$12 per night 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, the PAL partner will have completed \$338M in new construction and renovation by the end of FY14 en route to curing the full \$1.1B requirement by 2020.

Installation Savings: The low rates charged by Army Lodging were an illusion. There were significant government fixed 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 appropriated fund costs made it difficult for the government to understand and efficiently manage its all-in lodging expenses. Under privatization, there are no longer any hidden costs as the room rates represent the true cost of lodging.

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. The 75% of per diem rate covers the cost of

all former government subsidies and funds all recapitalization and sustainment requirements. The 25% official traveler discount represents an annual cost savings of \$86M compared to full per diem.

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, \$51 goes toward paying operating expenses, \$5 goes to the hotelier as a capped fee for service and \$44 goes into a lockbox used exclusively for Army-approved new construction, renovation and long-term sustainment requirements.

Taking Care of Employees: The PAL hotelier offers competitive wages and benefit packages to its employees. On the respective transition dates of the three PAL groups, there were 1,542 jobs to be filled. Of these jobs, 1,401 (91%) were filled with former Army Lodging employees, including 23 of the 39 general manager positions. In the words of former Army Lodging general manager, Gabriele Whitaker, on the occasion of the Fort Sill ribbon-cutting for the world's largest Holiday Inn Express hotel, "I have been working here for 19 years. I think it's the greatest thing that ever happened. Because to me, the Soldiers are finally getting the services they deserve and the amenities that they deserve."

Meeting the Mission: Four years into privatization, the PAL partner has accommodated trainees, foreign students, military families, wounded warriors, distinguished visitors, flight crews, business travelers, contractors, retirees – anyone and everyone that has needed to stay on-post in support of the mission. Feedback on privatization from Garrison Commanders and guests alike has been overwhelmingly positive. Government interests have been protected through the lease and any and all issues that have arisen have been adequately addressed through the Army's asset management program.

Proven Results: The Army's privatized lodging program is delivering on its promise. Occupancy and financial performance have been strong. Ribbon cuttings for renovated on-post Holiday Inn Express® hotels and groundbreaking ceremonies for new Candlewood Suites® are occurring with increasing regularity. Official travelers are enjoying enhanced service offerings, new amenities and frequency-stay points.

Lodging privatization offered the Army a means to recapitalize and sustain its on-post lodging inventory and save significant local installation support costs. As budget cuts drive the need for change and innovation, 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 assess the benefits of implementing their own lodging privatization programs.

For additional information on privatized DOD lodging, please contact:

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