

**A** *udit*



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DISPOSITION OF INSURANCE ALLOTMENT PAYMENTS

Report No. D-2001-147

June 21, 2001

Office of the Inspector General  
Department of Defense

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### **Acronyms**

DFAS	Defense Finance and Accounting Service
DFAS-CL	Defense Finance and Accounting Service Cleveland
DFAS-DE	Defense Finance and Accounting Service Denver
DFAS-IN	Defense Finance and Accounting Service Indianapolis
DFAS-KC	Defense Finance and Accounting Service Kansas City



INSPECTOR GENERAL  
DEPARTMENT OF DEFENSE  
400 ARMY NAVY DRIVE  
ARLINGTON, VIRGINIA 22202

June 21, 2001

MEMORANDUM FOR UNDER SECRETARY OF DEFENSE  
(COMPTROLLER)  
UNDER SECRETARY OF DEFENSE FOR  
PERSONNEL AND READINESS  
DIRECTOR, DEFENSE FINANCE AND  
ACCOUNTING SERVICE

SUBJECT: Audit Report on Disposition of Insurance Allotment Payments  
(Report No. D-2001-147)

We are providing this report for review and comment. We conducted the audit in response to a request from the Under Secretary of Defense for Personnel and Readiness. We considered comments from the Director, Defense Finance and Accounting Service, when preparing the final report.

DoD Directive 7650.3 requires that all recommendations be resolved promptly. The Director, Defense Finance and Accounting Service, comments were partially responsive. The Director did not comment on Recommendation 1.c. Therefore, we request the Director provide comments on Recommendation 1.c. in response to the final report. We request that the Director provide the comments by August 20, 2001.

We appreciate the courtesies extended to the audit staff. For additional information on this report, please contact Mr. Michael A. Joseph at (757) 766-9108 (mjoseph@dodig.osd.mil) or Ms. Betsy Brilliant at (703) 604-8875 (DSN 664-8875) (bbrilliant@dodig.osd.mil). See Appendix C for the report distribution. The audit team members are listed inside the back cover.

A handwritten signature in black ink, appearing to read "Thomas F. Gimble", is positioned above the typed name.

Thomas F. Gimble  
Acting  
Deputy Assistant Inspector General  
for Auditing

## Office of the Inspector General, DoD

Report No. D-2001-147  
(Project No. D2001LF-0010)

June 21, 2001

### Disposition of Insurance Allotment Payments

#### Executive Summary

**Introduction.** This audit was requested by the Under Secretary of Defense for Personnel and Readiness. The request was prompted by action taken by the Florida Department of Insurance against two life insurance companies that had received large numbers of insurance allotments from Service members through their servicing Defense Finance and Accounting Service (DFAS) sites. The insurance companies were required to return or escheat \$4.65 million that they had received over a 20-year period for canceled or non-existing insurance policies.

The DoD military pay system includes an allotment process that permits active duty and retired Service members to direct a portion of their pay to third parties. Payments for life, health, and other insurance premiums are valid allotments.

According to data for July through September 2000, DFAS distributed about \$25 million each month for approximately 350,000 insurance allotments. Although more than 400 insurance companies received allotments from DFAS during that period, 29 companies received more than 80 percent of the insurance allotment funds.

Allotment payments are sent to insurance companies by DFAS with a list of the individuals for whom the allotments apply. The insurance companies compare the list against their account records to identify “unmatched allotments.” Unmatched allotments are those allotments received by an insurance company for which the company does not have an insurance policy in effect or pending. Unmatched allotments can be further divided into two major types—allotments for canceled insurance policies and allotments for which the company has no record of a past, present, or pending relationship with the payer, also known as non-existing insurance policies.

**Objectives.** The overall objective of the audit was to evaluate the procedures used by insurance companies for disposing of or returning to Service members allotment payments for canceled or non-existing insurance policies. In addition, we reviewed DFAS procedures for establishing, monitoring, and stopping insurance allotments. We also reviewed the adequacy of the management control programs at the DFAS sites, as they applied to processing returned allotments.

**Results.** The seven insurance companies included in our review had procedures in place to identify and return allotments for canceled or non-existing policies. The insurance companies attempted to return allotment funds either directly to the Service members or to DFAS.

The four DFAS sites did not consistently process requests from insurance companies to stop insurance allotments. In addition, one DFAS site would not accept returned allotments from insurance companies. As a result, incorrect allotments may continue

for canceled and non-existing insurance policies, Service members' insurance coverage may be adversely affected, and Service members may not receive refunds in a timely manner. We could not quantify the number of incorrect allotments issued, because insurance companies do not send all incorrect allotments back to DFAS. However, based on the estimates of the insurance companies visited and our limited review of their documentation, we believe the number of incorrect allotments is relatively small—less than 1 percent of all allotments. However, despite the small percentage, the problem should be corrected because it involves Service members' pay and potentially their beneficiaries' entitlements. For details on the audit results, see the Finding section of the report. See Appendix A for a discussion of our review of the management control programs.

**Summary of Recommendations.** We recommend that the Director, DFAS, in coordination with the Under Secretary of Defense (Comptroller), issue standard procedural guidance to the DFAS sites requiring them to stop incorrect insurance allotments when a properly documented request is received from an insurance company, requiring them to accept returned allotments from insurance companies, and prohibiting them from sending returned allotments back to insurance companies. In addition, we recommend that the Director provide guidance to insurance companies that outlines the procedural requirements, including timelines, for requesting that allotments be stopped and for returning allotments to DFAS.

**Management Comments.** The Director, DFAS, concurred with the recommendations. The Director agreed to issue standardized guidance requiring DFAS sites to stop allotments when a properly documented request is received from an insurance company and to accept and process returned allotment payments. DFAS also agreed to establish procedures for returning allotments and to notify companies of the new procedures in October 2001. DFAS stated that it would also establish a 15-day time period for accepting returned allotments. Although not required to comment, the Deputy Under Secretary of Defense (Program Integration) reviewed the draft report and concurred with the finding and recommendations. See the Finding section for a discussion of management comments and the Management Comments section for the complete text of the comments.

**Audit Response.** The DFAS comments were partially responsive to the recommendations. DFAS did not comment on the recommendation to prohibit DFAS sites from sending returned allotments back to insurance companies. Although DFAS did not comment on the recommendation, a DFAS representative stated that she believed the problem would be solved by the prompt return of allotments by insurance companies. However, the insurance companies we visited generally returned unmatched allotments between 30 and 90 days. Accordingly, we request that DFAS provide comments on the recommendation. Specifically, DFAS should explain how it will prevent DFAS sites from sending returned allotments back to insurance companies, especially if the insurance companies do not meet the 15-day requirement. We request that the Director, DFAS, provide additional comments by August 20, 2001.

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## Background

This audit was requested by the Under Secretary of Defense for Personnel and Readiness. The request was prompted by action taken by the Florida Department of Insurance against two life insurance companies that had received large numbers of insurance allotments from Service members through their servicing Defense Finance and Accounting Service (DFAS) sites. The companies, American Fidelity Life Insurance Company and Trans World Assurance Company, had not appropriately returned allotments that could not be applied to current policies.<sup>1</sup>

**The Allotment System.** The DoD military pay system includes an allotment process that permits active duty and retired Service members to direct a portion of their pay to third parties. Payments for life, health, and other insurance premiums are valid allotments.

**Defense Finance and Accounting Service.** DFAS is responsible for processing and distributing active duty and retirees' military pay and allotments. The pay for each Service is handled by a different DFAS site. DFAS Indianapolis (DFAS-IN) handles Army pay; DFAS Cleveland (DFAS-CL) handles Navy pay; DFAS Denver (DFAS-DE) handles Air Force pay; and DFAS Kansas City (DFAS-KC) handles Marine Corps pay. DFAS-CL is also responsible for the pay of retirees from all the Services.

**Monthly Insurance Allotments.** According to data obtained from DFAS for July through September 2000, DFAS distributed about \$25 million each month for approximately 350,000 insurance allotments. More than 400 insurance companies received allotments from DFAS during that period. The exact number and amount of insurance allotments paid varies from month to month. In addition, because of the design of the allotment system, it is not possible to distinguish between allotments for life insurance and for other forms of insurance.

**Allotment Distribution.** Although more than 400 insurance companies received insurance allotments for each of the 3 months, 29 companies received more than 80 percent of the insurance allotment funds. As the following table illustrates, the top 20 companies for each DFAS site received more than 80 percent of the insurance allotment funds. For September 2000 allotments, the top 20 companies for each DFAS site were paid a total of \$20.7 million, accounting for 83 percent of the \$24.9 million paid for insurance allotments.

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<sup>1</sup>In February 2000, the Florida Department of Insurance issued Consent Orders requiring that the two insurance companies return or escheat \$4.65 million from allotments that the companies had received over a 20-year period for canceled or non-existing insurance policies. The Florida Department of Insurance found the companies had allowed erroneously received allotment funds to accumulate over two decades while making no substantial efforts to refund the money or otherwise resolve the situation.

<b>September 2000 Insurance Allotments</b>				
<u>Service</u>	<u>Number of Insurance Companies Paid</u>	<u>Number of Insurance Allotments Paid</u>	<u>Total Dollars (in millions)</u>	<u>Percent of Dollars to Top 20</u>
Army	369	129,029	\$9.11	83
Navy	320	83,629	5.93	86
Air Force	400	108,596	7.86	82
Marine Corps	204	25,282	2.04	82

**Processing Insurance Allotments.** Service members start, stop, or change insurance allotments by completing a DD Form 2558, “Authorization to Start, Stop, or Change an Allotment,” and submitting it to their local finance office. In addition to personal identifying information, the Service member includes the name, address, and account number of the insurance company. Local finance office personnel verify the information on the form and insert the DFAS-assigned company code.<sup>2</sup> Local finance office personnel then enter the data from the DD Form 2558 into the finance office’s computer system and the information is transmitted overnight to the Service’s DFAS site. The DFAS site’s computer system processes the transaction, implements the requested action, and notifies the local finance office that the transaction has been completed. The DFAS site also notifies the local finance office if the transaction cannot be processed.

**DFAS Allotment Payment Process.** For companies receiving more than 25 allotments per month, DFAS sends a blanket payment, either by electronic funds transfer or check, to a location designated by the insurance company, usually a financial institution. Simultaneously, the DFAS site sends a detailed list containing the Service member’s name, social security number, branch of Service, and amount for each allotment included in the blanket payment. The detailed list may be a magnetic tape, a computer file, or a hard-copy printout.

**Unmatched Allotments at Insurance Companies.** The insurance companies compare the DFAS list against their account records to identify “unmatched allotments.” There is no universal definition for unmatched allotments; however, for purposes of this report, we considered unmatched allotments to be those allotments received by an insurance company for which the company does not have a current or pending insurance policy. Unmatched allotments can be further divided into two major types—allotments for canceled insurance policies and allotments for which the company has no record of a past, present, or pending relationship with the payer, also known as non-existing insurance policies.

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<sup>2</sup>Because company codes are Service unique, each insurance company will have several company codes.

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## **Objectives**

The overall objective of the audit was to evaluate the procedures used by insurance companies for disposing of or returning to Service members allotment payments for canceled or non-existing insurance policies. In addition, we reviewed DFAS procedures for establishing, monitoring, and stopping insurance allotments. We also reviewed the adequacy of the management control programs at the DFAS sites, as they applied to processing returned allotments. See Appendix A for a discussion of the audit scope and methodology, our review of the management control programs, and prior coverage related to the audit objectives.

## **Results of Review**

The seven insurance companies included in our review had procedures in place to identify and return allotments for canceled or non-existing policies. The insurance companies attempted to return allotment funds either directly to the Service members or to DFAS. We limited the insurance companies that we visited to four of the top 29 companies that had not returned insurance allotments to DFAS in calendar year 2000, the two companies that prompted the audit, and the recipient of the largest dollar amount of allotments from DFAS. See Appendix B for a discussion of the procedures used by insurance companies for processing allotment payments and identifying and returning unmatched allotments. See the Finding section of the report for the results of our review of DFAS procedures for processing allotments.

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## Disposition of Unmatched Allotment Payments

The DFAS sites did not consistently process requests from insurance companies to stop insurance allotments. In addition, one DFAS site would not accept returned allotments from insurance companies. The inconsistencies in processing allotments occurred because there was no standardized guidance for stopping allotments or processing returned allotments from insurance companies. As a result, incorrect allotments may continue for canceled and non-existing insurance policies, Service members' insurance coverage may be adversely affected, and Service members may not receive refunds in a timely manner.

### Processing Insurance Allotments

The four DFAS sites did not consistently process requests from insurance companies to stop insurance allotments. In addition, although returned allotments were accepted, processed, and properly credited to Service members' accounts at three of the four DFAS sites, the fourth DFAS site would not accept returned allotments from insurance companies.

**DFAS Policies and Procedures.** The four DFAS sites developed the following local policies and procedures for processing allotments. The sites' guidance addresses all allotments and is not specific to insurance allotments.

**DFAS Indianapolis.** DFAS-IN did not have an official policy for stopping allotments or accepting returned allotments. However, it uses an undated "Remittance Team" standard operating procedure. The guidance, which includes a flowchart, outlines the steps to be taken for processing returned allotments and stopping allotments. The flowchart has a decision block that asks, "Did the company ask to have the allotment stopped?" If answered "yes," the next steps are to stop the allotment and input the reason for stopping the allotment. However, DFAS-IN will not stop an allotment until the allotment payment has been returned three times. The final step is to credit the Service member's account with the returned payment.

**DFAS Cleveland.** DFAS-CL policy is outlined in the "Allotments" chapter under the "Pay Topics" section of the Navy training manual for the Defense Joint Military Pay System, as revised November 9, 2000. The manual states that when an allotment is returned, an attempt will be made to correct the address, reissue the allotment to the correct allottee, or cancel the allotment. The DFAS-CL guidance does not specifically address requests to stop allotments or the handling of allotment payments returned by insurance companies. DFAS-CL personnel explained that they only stop allotments after they receive approval from the Service member through his or her finance office. When an allotment is returned by an insurance company, the money is immediately credited to the Service member's account.

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**DFAS Denver.** The DFAS-DE guidance is DFAS-DE Manual 7073-1, chapter 57, “Allotments of Pay,” January 15, 1998. The guidance provides that a request from the allottee (the insurance company) to stop an allotment does not require the signature of the Service member on a DD Form 2558. The guidance states that the allottee’s request or the return of funds to DFAS-DE serves as supporting documentation for stopping the allotment. Although the guidance does not specify when the allotment will be stopped, the unofficial policy is to stop the allotment only after receipt of three returned allotments from the insurance company. The guidance states that when an allotment is returned, the funds are credited to the Service member’s account and the allotment is corrected or stopped, as appropriate.

**DFAS Kansas City.** The DFAS-KC allotment guidance is DFAS-KC Regulation 7220.45-R, chapter 2, “Authorized Allotments,” October 20, 2000. However, the chapter does not address stopping allotments at the request of insurance companies or accepting or processing returned allotments. When DFAS-KC receives a returned allotment check from an insurance company with a request to stop the allotment, DFAS-KC will immediately stop the allotment, but will not accept the check. Instead, under procedures implemented in March 2000, DFAS-KC returns the check to the insurance company with notification that it is the insurance company’s responsibility to locate the member and refund the allotment directly.

**Processing Returned Allotments.** The three DFAS sites that accept returned allotments use basically the same procedures, which are as follow.

- An insurance company sends a check to DFAS with a list identifying each Service member with an unmatched allotment by name, social security number, and allotment amount.
- A DFAS collections branch employee logs in receipt of the check, copies the check and any accompanying documentation, deposits the check, and forwards a collection voucher with the documentation to the military pay branch.
- The military pay branch credits the amounts on the collection voucher to the Service members’ accounts.
- Allotment funds are returned to the insurance company only if the military pay branch cannot find an active pay account or a current address for an individual who has left the Service.

Although DFAS-KC indicated that processing returned allotments was a problem, none of the other three DFAS sites indicated that they had encountered any significant problems accepting, crediting, or accounting for returned allotments. To determine the level of effort required by a DFAS site to locate an individual, we contacted an insurance company for the name and social security number of a Service member for whom DFAS-KC had returned a check. We entered the social security number into a DoD database and obtained both the unit and personal mailing addresses in less than a minute.

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We recognize that not every case can be so easily resolved. However, we believe the DFAS sites are in a better position than the insurance companies to resolve the difficult cases.

Because the DFAS sites handle allotment stops and returns differently, insurance companies are unclear about DFAS procedures. Two of the companies we visited were not aware that DFAS would accept returned allotments and one did not know DFAS would stop allotments. One insurance company no longer returned allotments to DFAS because of concerns about the funds being credited to the Service members' accounts. Further, one insurance company reported that DFAS had agreed to stop an allotment for a very small dollar amount but had refused to stop other allotments when requested.

## **DoD and DFAS Guidance**

The inconsistencies in processing allotments occurred because there was no standardized guidance for stopping allotments or processing returned allotments from insurance companies. Each DFAS site developed its own unique operating policies and procedures. In addition, there was no guidance provided to the insurance companies regarding the procedures they should follow to request that an allotment be stopped or to return an unmatched allotment payment to DFAS.

**DoD Allotment Guidance.** The primary DoD guidance for allotment processing is DoD Regulation 7000.14-R, "DoD Financial Management Regulation," volume 7A, chapters 41 and 42, dated February 2000. The Regulation provides guidance as to the types of allotments authorized, who may authorize allotments, what pay can be allotted, and time periods for allotments to be paid. However, the DoD guidance does not include procedures for stopping allotments or accepting returned allotments from companies, except in the event of the death of the allotment payer or the recipient.

**DFAS Guidance.** Each DFAS site developed local guidance for processing both insurance company requests to stop allotments and returned allotments. However, some of the guidance is unofficial, and the guidance is not consistent among the DFAS sites. Further, the guidance does not adequately address what a DFAS site needs from the insurance companies regarding requests to stop allotments and regarding returned allotments.

**DoD-Wide Guidance Needed.** DFAS should develop specific guidance that requires all DFAS sites to stop incorrect allotments when requested by insurance companies, if the request is properly documented and justified. Stopping incorrect allotments would help limit the number of allotments repeatedly returned to DFAS. DFAS should also issue guidance that requires all DFAS sites to accept returned allotments from insurance companies. Accepting returned allotments would help ensure that Service members receive their refunds. DFAS sites return refunds to the insurance company if they cannot readily locate the Service member. However, we believe that practice should stop because Service members have a better chance of getting a refund from DFAS than from an insurance company with which they do not have a policy. Further, DFAS should provide guidance to the insurance companies that outlines

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the procedural requirements, including timelines, for returning allotments to DFAS. The insurance companies also reported that DFAS would not provide any written guidance on how to request that an allotment be stopped. Standardized guidance to the insurance companies would help them fix incorrect allotments and minimize delays in Service members' receiving refunds.

## **Effect of DFAS Procedures**

As a result of the lack of standardized guidance, incorrect allotments may continue for canceled and non-existing insurance policies, Service members' insurance coverage may be adversely affected, and Service members may not receive refunds in a timely manner. We could not quantify the number of incorrect allotments issued, because insurance companies do not send all incorrect allotments back to DFAS. However, based on the estimates of the insurance companies visited and our limited review of their documentation, we believe the number of incorrect allotments is relatively small—less than 1 percent of all allotments. However, despite the small percentage, the problem should be corrected because it involves Service members' pay and potentially their beneficiaries' entitlements.

**Allotments Continue.** When DFAS continues to issue incorrect allotments, Service members may believe they have insurance coverage when they do not. For example, if a member applied for insurance with one company and the allotment went to another company, the member could, in fact, have no coverage. However, the member's leave and earnings statement would indicate that he or she is paying for insurance. When DFAS stops the allotment, the member is notified on the leave and earnings statement and can take action to ensure insurance coverage. When the allotment is not stopped until three returned allotments are received, as done by two DFAS sites, the Service member may not be aware of the problem for several months.

Some insurance companies reported receiving incorrect allotments for several years because neither the Service member nor the DFAS sites would correct the allotment at the insurance company's request. DFAS-DE reported that it receives and acts on 10 to 15 requests per month from insurance companies to stop allotments. The DFAS-DE representative also stated that he had not received any negative feedback from Service members as a result of stopping an allotment.

**Timeliness of Refunds.** The inconsistent DFAS procedures may delay or even prevent the receipt of refunds by Service members. Although the DFAS sites do not routinely track and summarize returned insurance allotments, at our request, two DFAS sites compiled summaries of the number of returned allotments for a 1-year period. DFAS-IN reported it received 765 refund checks from insurance companies in calendar year 2000, but could not identify the exact number of Service members affected. DFAS-KC reported that it received 190 refund checks in calendar year 1999 that affected 765 Marines. The data from DFAS-KC indicated that most of the refunds were returned allotments from insurance companies. Under the procedures implemented at DFAS-KC in March 2000, the returned allotments from insurance companies

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would not have been accepted, unnecessarily delaying or preventing the Service members from receiving their money. The DFAS-KC procedures are counterproductive because some companies do not return allotments to a DFAS site if they can locate the Service member directly. As of March 22, 2001, one insurance company had already had DFAS-KC refuse to accept at least four returned allotments. Because that company only returns allotments to DFAS when it has had no prior contact with the payer, the Service members' refunds have been unnecessarily delayed.

## **Recommendations, Management Comments, and Audit Response**

**1. We recommend that the Director, Defense Finance and Accounting Service, in coordination with the Under Secretary of Defense (Comptroller), issue guidance to the Defense Finance and Accounting Service sites for processing allotments. At a minimum, the guidance should:**

**a. Require the sites to stop insurance allotments for canceled or non-existing insurance policies when a properly documented request is received from an insurance company.**

**b. Require the sites to accept returned allotments from insurance companies for canceled or non-existing insurance policies.**

**c. Prohibit the sites from sending returned allotments back to the insurance companies.**

**2. We recommend that the Director, Defense Finance and Accounting Service, provide guidance to all insurance companies that receive insurance allotments. The guidance should outline the procedural requirements, including timelines, for requesting that allotments be stopped and for returning allotments to the Defense Finance and Accounting Service sites.**

**Defense Finance and Accounting Service Comments.** DFAS concurred with Recommendation 1. DFAS stated that it would issue standard procedural guidance to DFAS sites requiring them to stop allotments when a properly documented request is received from an insurance company and requiring them to accept and process returned allotments. DFAS concurred with Recommendation 2. DFAS stated it would send notices to companies in October 2001 that any payment received by companies after October 2001 must be returned to DFAS within 15 business days after the date that it is received. Also, all identifying information (name, social security number, date, dollar amount, and account number) must accompany the returned item. DFAS stated that it will process the return as a refund to the member's pay account, notify the member, and stop the allotment.

**Audit Response.** The DFAS comments were partially responsive. DFAS did not comment on Recommendation 1.c. Although DFAS did not comment on this recommendation, a DFAS representative stated that she believed the

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problem of DFAS sites sending returned allotments back to insurance companies would be solved by the prompt return of allotments by insurance companies. However, as discussed in Appendix B, the insurance companies we visited generally returned unmatched allotments between 30 and 90 days. Accordingly, we request that DFAS provide comments on Recommendation 1.c. Specifically, DFAS should explain how it will prevent DFAS sites from sending returned allotments back to insurance companies, especially if the insurance companies do not meet the 15-day requirement.

**Deputy Under Secretary of Defense (Program Integration) Comments.**

Although not required to comment, the Deputy Under Secretary reviewed the draft report and concurred with the finding and recommendations.

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# Appendix A. Audit Process

## Scope and Methodology

**Work Performed.** We reviewed allotment policies dated January 1998 through November 2000 issued by the Under Secretary of Defense (Comptroller), the Services, DFAS headquarters, and the DFAS sites. We also reviewed insurance allotment data for the 3-month period of July through September 2000 and the allotment data for one insurance company for October 2000, as provided by DFAS. We visited local Army, Air Force, and Marine Corps installation finance offices and the four DFAS sites responsible for active duty Service members' pay. We also visited seven insurance companies that received allotments from DFAS.

At each local finance office, we discussed and examined the local procedures for accepting and entering the data to start, stop, or change allotments. At each DFAS site, we discussed procedures and reviewed documentation for handling requests to stop allotments and for processing returned allotments. We also verified that returned allotments had been properly credited to the Service members' accounts. At each DFAS site, we also examined documentation to determine the names of insurance companies from which it received returned allotments during calendar year 2000.

We limited our insurance company site visits based on the returned allotment information. As a result, we visited the following seven companies: two mutual aid associations that were among the top 20 recipients of allotments from two of the four DFAS sites;\* two companies that received large numbers of allotments but which had not returned allotments to the DFAS sites in calendar year 2000; the insurance company that received the largest dollar amount in allotments; and the two insurance companies that prompted the audit. The five insurance companies visited were among the top 20 recipients of insurance allotments from each DFAS site. In the context of this report, we included the two mutual aid associations when referring to insurance companies.

In September 2000, the seven companies we visited received a total of \$11.65 million, or 46.7 percent, of insurance allotment funds from DFAS. At each insurance company, we discussed the policies and procedures for identifying and returning allotments for canceled or non-existing insurance policies. We also discussed and examined error reports, suspense records, and other company-unique documents related to the audit objective. At one company we used random sampling to verify that allotments provided by DFAS had been properly credited to Service members' accounts.

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\*One of the associations supports the Army and Air Force and the other supports the Navy and Marine Corps.

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**Scope Limitation.** We did not visit a statistically valid sample of all insurance companies and only verified that allotment payments were being properly applied to Service members' accounts at one insurance company. Therefore, we cannot project or generalize the results. We did not quantify the number or dollar value of incorrect allotments at each insurance company because each company defines and categorizes incorrect allotments differently.

**DoD-Wide Corporate Level Government Performance and Results Act (GPRA) Coverage.** In response to the GPRA, the Secretary of Defense annually establishes DoD-wide corporate level goals, subordinate performance goals, and performance measures. This report pertains to achievement of the following corporate level goal and subordinate performance goal.

**FY 2001 DoD Corporate Level Goal 2:** Prepare now for an uncertain future by pursuing a focused modernization effort that maintains U.S. qualitative superiority in key warfighting capabilities. Transform the force by exploiting the Revolution in Military Affairs, and reengineer the Department to achieve a 21st century infrastructure. **(01-DoD-2)**

**FY 2001 Subordinate Performance Goal 2.5:** Improve DoD financial and information management. **(01-DoD-2.5)**

**DoD Functional Area Reform Goals.** Most major DoD functional areas have also established performance improvement reform objectives and goals. This report pertains to achievement of the following Financial Management functional area objective and goal.

**Objective:** Reengineer business practices. **Goal:** Revise regulations and procedures to simplify, standardize, and improve financial management requirements. **(FM-2.2)**

**High Risk Area.** The General Accounting Office has identified several high risk areas in the DoD. This report provides coverage of the DoD Financial Management high risk area.

**Use of Computer-Processed Data.** Our reliance on computer-processed data was limited to identifying insurance companies that received allotments and the number and dollar amounts received by each company for the period of July through September 2000. In addition, we received from DFAS detailed allotment data for one insurance company for October 2000. We did not perform a formal reliability assessment of the DFAS systems that produced the data. Because the sample data were only used to identify and rank insurance companies, and no projections or conclusions are based on the data, data reliability had no effect on the audit finding.

**Use of Technical Assistance.** Personnel in the Quantitative Methods Division, Audit Followup and Technical Support Directorate, Office of the Assistant Inspector General for Auditing, provided technical support for this audit. Operations research analysts selected the samples of individual allotments to track through the insurance company's records to verify the accuracy of account postings from allotments.

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**Audit Type, Dates, and Standards.** We performed this economy and efficiency audit from October 2000 through mid-April 2001 in accordance with auditing standards issued by the Comptroller General of the United States, as implemented by the Inspector General, DoD. Accordingly, we included tests of management controls considered necessary. Although we did our work in accordance with generally accepted Government auditing standards, we were unable to obtain an opinion on our system of quality control. The most recent external quality control review was withdrawn on March 15, 2001, and we will undergo a new review.

**Contacts During the Audit.** We visited or contacted individuals and organizations within DoD and at insurance companies. Further details are available upon request.

## Management Control Program Review

DoD Directive 5010.38, "Management Control (MC) Program," August 26, 1996, and DoD Instruction 5010.40, "Management Control (MC) Program Procedures," August 28, 1996, require DoD organizations to implement a comprehensive system of management controls that provides reasonable assurance that programs are operating as intended and to evaluate the adequacy of the controls.

**Scope of Review of Management Control Program.** We reviewed the adequacy of DFAS management controls over the processing of returned insurance allotments. Specifically, at each DFAS site, we reviewed management controls over receipt of returned allotments from insurance companies and crediting refunds to Service members' accounts. We reviewed management's self-evaluations applicable to those controls.

**Adequacy of Management Controls.** We did not identify a material management control weakness for DFAS, as defined by DoD Instruction 5010.40. However, we did identify a problem that needs to be corrected because it affects Service members' pay and benefits. The DFAS management controls for establishing policies and procedures were not adequate to ensure that the DFAS sites uniformly stop incorrect allotments and accept returned allotments for canceled or non-existing insurance policies. Recommendation 1., if implemented, will clarify and standardize DFAS allotment procedures.

**Adequacy of Management's Self-Evaluation.** Officials at DFAS-DE and DFAS-KC identified allotment processing as part of an assessable unit. However, in their self-evaluations, DFAS-DE and DFAS-KC officials did not identify the weakness identified by the audit because their management control plans do not specifically address returned allotments. Officials at DFAS-CL and DFAS-IN did not identify the control weakness identified by the audit because they did not identify allotment processing as an assessable unit in their management control plans.

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## **Prior Coverage**

Inspector General, DoD, Report No. 99-106, "Commercial Life Insurance Sales Procedures in DoD," March 10, 1999

Deputy Under Secretary of Defense (Program Integration) Report, "Final Report Insurance Solicitation Practices on Department of Defense Installations," May 15, 2000

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## Appendix B. Procedures Used by Life Insurance Companies to Process Allotments

The seven insurance companies visited had procedures for identifying and returning unmatched allotments. All of the insurance companies visited had some unmatched allotments. In addition, the 26 insurance companies\* that were the top 20 recipients of insurance allotments from DFAS-IN, DFAS-CL, and DFAS-DE all returned allotments for canceled or non-existing policies either directly to Service members or to a DFAS site in calendar year 2000.

**Identifying Unmatched Allotments.** Although detailed procedures and terminology vary among insurance companies, all the companies we visited identified unmatched allotments in basically the same manner. Each company maintains their customer accounts on computer systems that identify policyholders by social security number. When the company receives the detailed allotment information from DFAS, the company matches the social security numbers on the detailed listings with social security numbers in its current account files and credits premiums, as appropriate. For companies receiving large numbers of allotments, the initial match is done through the computer systems. If the detailed listing from DFAS contains social security numbers that are not in the company's current account files, an error or exception report is generated. The error report may also include cases where the social security number matches but the dollar amount of the allotment differs from the premium amount due according to the company's files, generally referred to as mismatched allotments.

**Reconciling Unmatched and Mismatched Allotments.** Each of the insurance companies visited had personnel responsible for reconciling unmatched and mismatched allotments, as identified by monthly error reports.

**Unmatched Allotments.** For unmatched allotments, insurance company personnel check both the "pending" business files, to determine whether an application is pending, and the "history" files, to determine whether the payer has canceled a policy. Personnel also cross-check names and addresses and check for "near match" social security numbers. Insurance company personnel estimated that they resolve more than 90 percent of the unmatched allotments on the original error report through reconciliation procedures. The remaining allotments require further investigation or action either using credit report services or some other research method.

**Mismatched Allotments.** Mismatched allotments can be either overpayments or underpayments of insurance policy premiums. For overpayments, the companies visited apply the appropriate amount to premiums and periodically return the excess to the Service member. For underpayments, the companies apply the amount received to the premium, creating an account

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\*Three insurance companies of the 29 that constituted the top 20 companies were unique to the Marine Corps' top 20. Marine Corps pay is handled by DFAS-KC. Because DFAS-KC did not accept returned allotments, we did not verify whether those three companies returned allotments to DFAS in 2000.

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shortage. Generally, the insurance companies visited do not contact the DFAS sites to correct the problem. Instead, they notify the Service members of the allotment mismatch and request that the members contact their finance offices to correct the allotment amount.

**Returning Unmatched Allotments.** The insurance companies use various procedures to return unmatched allotments to Service members. Of the 26 insurance companies that were the top 20 recipients of allotments from DFAS-IN, DFAS-CL, and DFAS-DE, 22 had returned allotments to 1 or more of the DFAS sites during calendar year 2000. The remaining four companies (two mutual aid associations and two insurance companies) had refunded unmatched allotments directly to the payers.

The seven insurance companies we visited provided the following information concerning their returned allotment procedures.

- The insurance company that received the largest dollar amount for all insurance allotments refunds most overpayments and payments on canceled policies directly to the payers. If the company cannot find the payer within 90 days, the unmatched allotments are returned to DFAS.
- The two companies that prompted this audit return unmatched allotments to DFAS. Allotments for canceled policies are returned within 30 days and those for non-existing policies are returned within 90 days. Additionally, the companies immediately refund overpayments directly to the Service members.
- One insurance company that had not returned allotments to DFAS in 2000 attempts to refund all mismatched and unmatched allotments directly to the payers. The company stated it sends a small number of allotments back to DFAS about once a year, but had not done so in 2000. A company official noted that his company had a small number of allotments that had not been returned. As of April 5, 2001, the company was holding \$292.55 in suspense for an unmatched allotment that it continued to receive. The official stated that he would welcome clear guidance from DFAS on returning allotments.
- The two mutual aid associations refund unmatched allotments and overpayments directly to the Service members. Representatives of both mutual aid associations stated they were not aware that they could return allotments to DFAS. As of April 5, 2001, one mutual aid association reported that it had \$870.55 in suspense for an unmatched allotment that began in December 2000. The other mutual aid association reported that it did not have any unmatched allotments that were more than 90 days old.
- The remaining insurance company also refunds unmatched allotments directly to the Service members. A company representative stated the company had stopped returning allotments to DFAS in 1994 because of concerns about returned allotments being credited to the Service members' accounts. As of April 5, 2001, the insurance company was holding \$1,467 in suspense for unmatched allotments.

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The suspense account information was provided by the insurance companies and was not validated by the audit team.

**Locating Payers of Unmatched Allotments.** The four companies that attempt to refund all unmatched allotments to the Service members use various methods to find a member's address. One company refers the social security numbers and names to its home office and its agents, two companies use commercial locator services, and one company has in-house personnel who conduct the searches. Any unmatched allotments not returned to either DFAS or a Service member ultimately have to be escheated to the State, per State law. Insurance companies try to refund as much money as possible of unmatched allotments to the Service member either directly or through DFAS, rather than escheat the funds.

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## **Appendix C. Report Distribution**

### **Office of the Secretary of Defense**

Under Secretary of Defense (Comptroller)  
Deputy Chief Financial Officer  
Deputy Comptroller (Program/Budget)  
Under Secretary of Defense for Personnel and Readiness

### **Department of the Army**

Auditor General, Department of the Army

### **Department of the Navy**

Naval Inspector General  
Auditor General, Department of the Navy

### **Department of the Air Force**

Assistant Secretary of the Air Force (Financial Management and Comptroller)  
Auditor General, Department of the Air Force

### **Other Defense Organizations**

Director, Defense Finance and Accounting Service

### **Non-Defense Federal Organization**

Office of Management and Budget

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## **Congressional Committees and Subcommittees, Chairman and Ranking Minority Member**

Senate Committee on Appropriations  
Senate Subcommittee on Defense, Committee on Appropriations  
Senate Committee on Armed Services  
Senate Committee on Governmental Affairs  
House Committee on Appropriations  
House Subcommittee on Defense, Committee on Appropriations  
House Committee on Armed Services  
House Committee on Government Reform  
House Subcommittee on Government Efficiency, Financial Management, and Intergovernmental Relations, Committee on Government Reform  
House Subcommittee on National Security, Veterans Affairs, and International Relations, Committee on Government Reform  
House Subcommittee on Technology and Procurement Policy, Committee on Government Reform

# Defense Finance and Accounting Service Comments



DFAS-DFM

## DEFENSE FINANCE AND ACCOUNTING SERVICE

1931 JEFFERSON DAVIS HIGHWAY  
ARLINGTON, VA 22240-5291  
WWW.DFAS.MIL

JUN 6 2001



MEMORANDUM FOR DIRECTOR, READINESS AND LOGISTICS  
SUPPORT DIRECTORATE, INSPECTOR GENERAL,  
DEPARTMENT OF DEFENSE

SUBJECT: Response to Draft Audit Report on Disposition of  
Insurance Allotment Payments (Project No. D2001LF-0010)

In response to the subject memorandum dated April 19, 2001, the Defense Finance and Accounting Service (DFAS) concurs with the recommendation that DFAS issue standard procedural guidance. Guidance will be issued to all DFAS sites requiring them to stop allotments when a properly documented request is received from an insurance company and requiring them to accept and process returned allotment payments. Concerning misdirected payments, we will send notices to companies in October 2001. Any payment received by companies after October 2001 must be returned to DFAS within 15 business days after the date it is received. All identifying information (name, social security number, date, dollar amount, and account number) must accompany the returned item. DFAS will process the return as a refund to the member's pay account, notify the member and stop the allotment.

Please refer any questions to my point of contact Ms. Ann Cook. She may be reached at (703) 607-5059 or email at [ann.cook@dfas.mil](mailto:ann.cook@dfas.mil).

Thomas R. Bloom  
Director

# Deputy Under Secretary of Defense (Program Integration) Comments



PERSONNEL AND  
READINESS

OFFICE OF THE UNDER SECRETARY OF DEFENSE  
4000 DEFENSE PENTAGON  
WASHINGTON, D.C. 20301-4000



MAY 31 2001

MEMORANDUM FOR DIRECTOR, READINESS AND LOGISTICS  
SUPPORT DIRECTORATE, INSPECTOR GENERAL,  
DEPARTMENT OF DEFENSE

SUBJECT: Audit Report on Disposition of Insurance Allotment Payments  
(Project No. D2001LF-0010)

We have reviewed the subject draft audit report and concur with its finding and  
associated recommendations.

Jeanne B. Fites  
Deputy Under Secretary of Defense  
(Program Integration)



## **Audit Team Members**

The Readiness and Logistics Support Directorate, Office of the Assistant Inspector General for Auditing, DoD, prepared this report. Personnel of the Office of the Inspector General, DoD, who contributed to the report are listed below.

Shelton R. Young  
Michael A. Joseph  
Betsy Brilliant  
R. Thomas Briggs  
W. Sterling Malcolm  
Daniel S. Bowers  
Lusk F. Penn  
James Hartman