



UNITED STATES GENERAL ACCOUNTING OFFICE
WASHINGTON, D.C. 20548

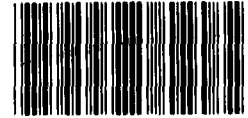
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NATIONAL SECURITY AND
INTERNATIONAL AFFAIRS DIVISION

B-207093

JULY 9, 1985

The Honorable Caspar W. Weinberger
The Secretary of Defense



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Dear Mr. Secretary:

Subject: Savings Can Be Realized If Nonappropriated Fund
Instrumentalities Pay For Their Unemployment
Costs (GAO/GGD-85-51)

We are currently conducting a review of unemployment benefit payments to former federal employees. Our review is not yet complete, but we have identified an opportunity that we believe could save the Department of Defense (DOD) several million dollars in appropriated funds each year. DOD can realize these savings by requiring its nonappropriated fund instrumentalities (NAFI)--morale, welfare, and recreation activities--to pay their own unemployment costs. About \$22 million in unemployment benefits have been paid to former DOD NAFI employees since fiscal year 1982.

DOD NAFIs include movie theaters, gasoline stations, clubs, golf courses, exchanges, and other recreational facilities and programs. According to a DOD official, DOD's 22,000 NAFIs employ about 205,000 people and during fiscal year 1983, generated about \$7.8 billion from the sale of goods and services to military customers.

DOD's overall policy is to reduce the scope and magnitude of appropriated fund support for NAFI activities. Requiring that NAFI-generated funds, rather than appropriated funds, be used to pay unemployment benefit costs for former NAFI employees would be consistent with this overall policy and with DOD's existing requirement that the NAFIs pay all other employee fringe benefit costs. Moreover, other federal agencies that have NAFI activities require the NAFIs to pay for their former employees' unemployment benefits. Such a change could also provide an incentive for NAFI managers to find ways to reduce their unemployment costs.

(966197)

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OBJECTIVES, SCOPE, AND METHODOLOGY

The objective of our on-going review is to identify ways that federal agencies can reduce unemployment costs through improved personnel and financial management practices. During November and December 1984, we gathered information on DOD NAFI operations from officials in the following DOD offices: (1) the Assistant Secretary of Defense for Manpower, Installations and Logistics, (2) General Counsel, and (3) the Comptroller. To obtain additional information on NAFI operations, we reviewed the DOD NAFI personnel policy manual, a November 1984 DOD consultant's study on NAFI unemployment costs,¹ and DOD's appropriation acts for fiscal years 1982 through 1985. We also contacted Department of Labor officials who are responsible for administering the unemployment compensation program as well as officials at four agencies with NAFI activities: the Veterans Administration and the departments of Agriculture, State, and Transportation.

BACKGROUND

Since January 1, 1955, federal civilian employees have had unemployment insurance protection under Chapter 85, Title 5, of the U.S. Code, 5 U.S.C. § 8501 *et seq.* NAFI employees are also covered by this statute. In addition, Public Law 96-499, the Omnibus Reconciliation Act of December 5, 1980, which amended chapter 85, requires each federal agency to pay the cost of unemployment benefits for their eligible former employees (5 U.S.C. 8501, 8509). Before the 1980 legislation was enacted, the Department of Labor paid all agencies' unemployment costs (including the costs for DOD's NAFI personnel).

The eligibility requirements for unemployment compensation and the level of benefits payable to former federal employees are generally governed by the laws of the states in which the employee's last official duty station was located. The Department of Labor administers the unemployment compensation program for federal employees through agreements with each of the states. Under the program, an unemployed worker files a claim with the state. After verifying employment and wage data with the former employing agency, the state determines the employee's eligibility and the amount of benefits. States bill the Department of Labor each quarter for all benefits paid to former employees of each federal agency. Labor then bills each

¹Study of Unemployment Compensation Policy for Nonappropriated Fund Employees performed for the Assistant Secretary of Defense for Manpower, Installations, and Logistics.

federal agency. The agency pays the bill by transferring funds to a Department of Treasury account from which states draw funds to pay benefits to former federal employees.

CONGRESSIONAL COMMITTEE
DIRECTED DOD TO STOP USING
APPROPRIATED FUNDS TO PAY
NAFI UNEMPLOYMENT COSTS

The House Appropriations Committee report on DOD's supplemental budget request for fiscal year 1982 stated that it was inappropriate for DOD to use appropriated funds to pay NAFI unemployment costs, recommended that funds DOD had requested for NAFI unemployment be deleted, and directed DOD to develop a reasonable estimate of NAFI unemployment costs and to use NAFI-generated funds to pay these costs. The Senate Appropriation Committee agreed with the House reduction and also deleted the funds from DOD's budget. In May 1982, a DOD official told the House Appropriations Subcommittee on Defense that current accounting procedures did not provide a sufficient level of detail to identify NAFI unemployment costs. Therefore, DOD continued using appropriated funds to pay the costs. (The 1982 Defense Appropriation Act did not prohibit DOD from using appropriated funds to pay NAFI unemployment costs.) The House and Senate Appropriations Committees' reports for fiscal years 1983 through 1985 did not mention NAFI unemployment costs.

In May 1983, DOD informed the House Subcommittee that it did not agree that DOD should use NAFI-generated funds, rather than appropriated funds, to pay for NAFI unemployment costs. DOD told the committee that before the Omnibus Reconciliation Act of 1980 the Department of Labor used appropriated funds to pay NAFI unemployment costs. Accordingly, DOD did not believe it was appropriate to change this practice merely because the Congress passed a law that requires DOD, rather than Labor, to pay for DOD's unemployment costs. During our review, an official from DOD's General Counsel's office told us that DOD's position on this issue has not changed. As of January 1985, DOD was still using appropriated funds to pay NAFI unemployment costs.

DOD CAN IDENTIFY NAFI
UNEMPLOYMENT COSTS

In March 1981, the Department of Labor assigned unique account numbers to all federal agencies (including DOD NAIs) so that states could separately identify all unemployment benefits paid to each agency's former employees. And, as shown in Enclosure I, states have submitted bills to the Department of

Labor showing that benefits paid to former DOD NAFI employees since fiscal year 1982 have totaled about \$22 million.

During our review, a DOD Comptroller official told us that although NAFI unemployment costs are available in the aggregate, the Department of Labor did not assign unique account numbers to each of the 22,000 NAFIs and that, as a result, current accounting procedures did not provide a sufficient level of detail to identify the actual unemployment costs for each NAFI.

We believe this lack of detail would not preclude DOD from paying unemployment costs with NAFI-generated funds. Most NAFI-generated funds are transferred to the military services' headquarters activities for central management. The service headquarters could use these centrally managed funds to pay NAFI unemployment costs. A similar suggestion, which DOD has not acted on, was made in the November 1984 DOD consultant's study, which recommended that Army NAFI unemployment bills be paid by the Army Adjutant General. The Adjutant General could then opt to charge or not charge these costs back to the individual NAFIs. The study pointed out further that an Army NAFI official believed that NAFI central payroll office computer systems could be modified to identify the actual unemployment costs for each NAFI.

DOD'S POLICY IS TO REDUCE
APPROPRIATED FUND SUPPORT
OF NAFI

If DOD were to change its current policy and begin charging NAFIs for their unemployment costs, it would help DOD to achieve its overall objective of reducing the amount of appropriated funds currently used to support NAFI operations. DOD's directive on funding of morale, welfare, and recreation programs (DOD 1015.6) states that the heads of DOD components shall "within the guidelines provided in this Directive, exert continuing efforts at all echelons to minimize the scope and magnitude of appropriated fund support." Appropriated funds are sometimes used to pay for certain support functions for NAFI operations. However, it is DOD's policy that NAFI-generated funds be used to pay NAFI civilian personnel.

Unemployment insurance is a fringe benefit to which NAFI employees are entitled. DOD currently requires NAFIs to pay all other personnel fringe benefit costs. DOD's personnel policy manual for NAFIs (DOD 1401.1M) states that "no appropriated funds will be requested or expended in connection with life insurance, medical, retirement, or survivor benefits established or authorized by this manual."

NAFI MANAGERS WOULD HAVE
AN INCENTIVE TO ANALYZE
UNEMPLOYMENT CLAIMS

In our opinion, using DOD appropriated funds to pay NAFI unemployment costs constitutes a subsidy of NAFIs that may lessen the incentive for NAFI managers to carefully analyze unemployment claims. This point was also made in the consultant's November 1984 study of DOD's unemployment costs for NAFI personnel. This study stated that an official from one state unemployment office believes that there is a lack of accountability among NAFI personnel officials:

"He feels large sums of money are being wasted because NAF personnel are not appealing questionable claims. He feels that personnel are not making appeals presently because there is no incentive to do so (they know reimbursement is from appropriated funds) and because most NAF components also feel that it is not 'cost effective'."

OTHER FEDERAL AGENCIES DO
NOT USE APPROPRIATED FUNDS
TO PAY NAFI UNEMPLOYMENT COSTS

We contacted four federal agencies that have NAFI activities--the Veterans Administration and the departments of Agriculture, State, and Transportation--to determine what their policies were for paying NAFI unemployment costs. Officials from all four agencies told us they do not use appropriated funds to pay NAFI unemployment costs; NAFI-generated funds are used to pay these costs. Prior to the Omnibus Reconciliation Act of 1980, Labor used appropriated funds to pay these agencies' NAFI unemployment costs.

CONCLUSIONS

We believe DOD should use NAFI-generated funds, rather than appropriated funds, to pay NAFI unemployment costs. Using NAFI-generated funds for this purpose would be consistent with (1) the House Appropriation Committee's 1982 directive, (2) DOD's general policy to find ways to reduce appropriated fund support to NAFIs, (3) DOD's current policy to charge NAFIs for other personnel fringe benefits costs, and (4) the policies of other agencies that operate NAFIs. Charging NAFIs for their unemployment costs would also save DOD several million dollars in appropriated funds each year, eliminate a taxpayer subsidy of NAFI operations, and provide an incentive for NAFI managers to better analyze unemployment benefit claims.

RECOMMENDATION

We recommend that the Secretary of Defense require that NAFI-generated funds be used to pay for unemployment benefits received by former NAFI employees.

AGENCY COMMENTS


On March 25, 1985, we provided a draft of this report to DOD for review and comment. On May 31, 1985, DOD agreed with our recommendation and stated that, beginning in fiscal year 1986, it would charge the military services' central NAFI funds for the unemployment costs incurred by each service's NAFIs. In addition, DOD stated that, beginning in fiscal year 1987, it would require each service's central NAFI fund to allocate its total unemployment costs to individual NAFIs. (See Enc. II.)

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As you know, 31 U.S.C. 720 requires the head of a federal agency to submit a written statement on actions taken on our recommendations to the Senate Committee on Governmental Affairs and the House Committee on Government Operations not later than 60 days after the date of the report and to the House and Senate Committees on Appropriations with an agency's first request for appropriations made more than 60 days after the date of the report.

We are sending copies of this report to the Chairmen of the House and Senate Committees on Appropriations and the cognizant legislative committees; the Secretary of Labor; the Director, Office of Management and Budget; and other interested parties.

Sincerely yours,


for Frank C. Conahan
Director

Enclosures - 2

Table 1

Unemployment Benefits Paid To Former
DOD NAFI Personnel

DOD Component	Fiscal Years			First Qtr. 1985 ^a	Total
	1982 ^a	1983 ^a	1984 ^a		
Army	\$ 935,378	\$1,540,498	\$1,761,916	435,442	\$4,673,234
Navy	1,217,353	2,285,420	1,996,394	312,255	5,811,422
Air Force	944,613	1,605,245	1,496,172	310,819	4,356,849
AAFES ^b	<u>1,565,398</u>	<u>2,976,238</u>	<u>2,320,773</u>	<u>489,662</u>	<u>7,352,071</u>
Total	<u>\$4,662,742</u>	<u>\$8,407,401</u>	<u>\$7,575,255</u>	<u>\$1,548,178</u>	<u>\$22,193,576</u>

Source: Department of Labor's Employment and Training Administration.

^aAs of May 2, 1985, 13 states had not submitted complete bills for payments made to former NAFI personnel for fiscal years 1981 through the first quarter of fiscal year 1985. One state that has not submitted any bills since the second quarter of fiscal year 1982 has many NAFI activities. After all states submit complete bills, it is probable that DOD's actual NAFI unemployment costs will exceed the amounts shown.

^bArmy and Air Force Exchange Service.



THE ASSISTANT SECRETARY OF DEFENSE

WASHINGTON, D. C. 20301-4000

MANPOWER,
INSTALLATIONS
AND LOGISTICS

May 31, 1985

Mr. Frank C. Conahan
Director, National Security and
International Affairs Division
U.S. General Accounting Office
Washington, DC 20548

Dear Mr. Conahan:

This is the Department of Defense response to the General Accounting Office (GAO) draft report, GAO Code No. 966197, OSD Case No. 6717, entitled "Charging Nonappropriated Fund Instrumentalities For Their Unemployment Costs Can Save Millions In Appropriated Funds."

In the report, the GAO points out that it is existing DoD policy that the heads of DoD components minimize the scope and magnitude of appropriated fund support to the DoD morale, welfare and recreation program, that the House Appropriations Committee had stated it was inappropriate for DoD to use appropriated funds to pay for NAFI unemployment costs and that other Federal agencies which have nonappropriated fund instrumentalities use NAFI generated funds to pay related unemployment costs. The DoD concurs in these findings and positions.

Detailed DoD comments addressing each of the findings and the recommendation contained in the draft report are in the enclosure to this letter. DoD appreciates the opportunity to comment on the draft report.

Sincerely,

Enclosure

GAO DRAFT REPORT - DATED MARCH 25, 1985
(GAO CODE NO. 966197) - OSD CASE NO. 6717

"CHARGING NONAPPROPRIATED FUND INSTRUMENTALITIES FOR THEIR
UNEMPLOYMENT COSTS CAN SAVE MILLIONS IN APPROPRIATED FUNDS"

DOD RESPONSES TO FINDINGS AND RECOMMENDATION TO BE ADDRESSED
IN THE GAO DRAFT REPORT

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FINDINGS

FINDING A: Use of Nonappropriated Fund Instrumentalities
For Unemployment Benefit Costs Could Save Millions Annually.

GAO reported that since January 1, 1955, Federal civilian employees and nonappropriated fund instrumentalities (NAFI) employees have had unemployment insurance protection under Chapter 85, Title 5, of the U.S. Code, 5 U.S.C. GAO concluded that, since it is DoD's overall policy to reduce the scope and magnitude of appropriated fund support for NAFI, requiring that NAFI-generated funds, rather than appropriated funds, be used to pay unemployment benefit costs for former NAFI employees would be consistent with this policy, as well as with DoD's existing requirement that the NAFIs pay all other employee fringe benefit costs. GAO also noted it is the policies of other agencies that operate NAFIs for NAFI funds to be used for unemployment benefits. GAO further concluded that charging NAFIs for their unemployment costs would save DoD several millions in appropriated funds each year, eliminate a taxpayer subsidy of NAFI operations, and provide an incentive for NAFI managers to better analyze unemployment benefit claims. (pp. 1, 5, GAO Draft Report)

DoD RESPONSE: DoD concurs. It is noted, however, that unemployment insurance protection has not heretofore been considered an employee fringe benefit per se, but rather part of the cost of doing business.

FINDING B: Congress Directed DoD To Stop Using Appropriated Funds To Pay NAFI Unemployment Costs. GAO noted that the House Appropriations Committee report on DoD's supplemental budget request for FY 1982 stated that it was inappropriate for DoD to use appropriated funds to pay NAFI unemployment costs. GAO also noted that the Committee deleted the funds that DoD had requested for NAFI unemployment and directed DoD to develop a reasonable estimate of unemployment costs and use NAFI generated funds to pay these costs. GAO found, however, that in May 1983, DoD informed the House Subcommittee that it did not agree, that prior to the Omnibus Reconciliation Act of 1980, the Department of Labor (DOL) used appropriated funds to pay NAFI unemployment costs, and that DoD did not believe it was appropriate to change this practice merely because Congress passed a law requiring DoD, instead of DOL, to pay for DoD's unemployment costs. GAO also found that as of January 1985, DoD was still using appropriated funds to pay NAFI unemployment costs. GAO concluded that this was not consistent with the Committee's 1982 directive. (pp. 3 GAO Draft Report)

DoD RESPONSE: DoD concurs.

FINDING C: DoD Can Identify NAFI Unemployment Costs. GAO found that in March 1981, the DOL assigned unique account numbers to all Federal agencies so that states could separately identify all unemployment benefits paid to each agency's former employees. GAO noted DoD's statement that, although NAFI unemployment costs are available in the aggregate, the DOL did not assign unique account numbers to each of the 22,000 NAFIs and, as a result, current accounting procedures did not provide a sufficient level of detail to identify the actual unemployment costs for each NAFI. GAO concluded, however, that the lack of detail would not preclude DoD from paying unemployment costs with NAFI-generated funds because most NAFI-generated funds are transferred to the Military Services' headquarters activities for central management and the Services, in turn, could use these centrally managed funds to pay NAFI unemployment costs. (pp. 3-4 GAO Draft Report)

DoD RESPONSE: DoD concurs. As noted by GAO, however, the number of nonappropriated fund instrumentalities in being throughout the Department of Defense is in the thousands. In order to be most effective as GAO indicates, i.e., "... provide an incentive for NAFI managers to better utilize unemployment benefit claims," the ability to bill each fund for these unemployment costs incurred by former employees is highly desirable. The GAO alternative, i.e., pay unemployment costs with NAFI generated funds transferred to the Military Services' headquarters activities or central management, does not provide the basis for improving management because it does not impact at the level where the costs were generated.

FINDING D: DoD's Policy Is To Reduce Appropriated Fund Support Of NAFI. GAO noted that the DoD's directive on funding morale, welfare, and recreation programs (DoD Directive 1015.6) states that the heads of DoD components shall "within the guidelines provided, exert continuing efforts at all echelons to minimize the scope and magnitude of appropriated fund support." GAO found, however, that DoD, uses appropriated funds to pay NAFI unemployment costs contrary to its policy, and this constitutes a subsidy of NAFIs that may lessen the incentive of NAFI managers to carefully analyze unemployment claims. GAO further found that four other federal agencies it contacted--the Veterans Administration and the Departments of Agriculture, State, and Transportation--do not use appropriated funds to pay NAFI unemployment costs, but instead use NAFI-generated funds to pay the costs. GAO concluded that if DoD were to change its current policy and begin charging NAFIs for their unemployment costs, it would help DoD achieve its overall objective of reducing the amount of appropriated funds currently used to support NAFI operations and save several million dollars in appropriated funds. (pp. 4 GAO Draft Report)

DoD RESPONSE: DoD concurs.

RECOMMENDATION: GAO recommended that the Secretary of Defense require NAFI-generated funds be used to pay for unemployment benefits received by former NAFI employees. (p. 6, GAO Draft Report)

DoD RESPONSE: DoD concurs. As noted by the GAO - there are thousands of nonappropriated fund instrumentalities world-wide. To use nonappropriated funds to pay unemployment costs for former NAF employees is concurred in. However, to make the most use of this change in policy and in improving NAF management it is highly desirable that appropriate unemployment costs be charged to each appropriate NAFI. In order to develop and implement a system which will enable this to be performed will require significant effort on the part of each DoD component which administers NAFIs. Therefore, the effective date for such system implementation will be 1 October, 1986 - the beginning of fiscal year 1987. As an interim measure for FY 1986, the Department will charge the Military Services' central NAFI funds for the unemployment costs incurred by each service's NAFIs.

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