Final Audit Report

Subject:


Report No. 2A-II-00-09-065

Date: July 20, 2010

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AUDIT REPORT

Federal Employee Group Life Insurance Program
Contract No. 17000-G
Metropolitan Life Insurance Company
Oriskany, New York and Bridgewater, New Jersey

REPORT NO. 2A-II-00-09-065

DATE: July 20, 2010

Michael R. Esser
Assistant Inspector General for Audits
EXECUTIVE SUMMARY

Federal Employee Group Life Insurance Program
Contract No. 17000-G
Metropolitan Life Insurance Company
Oriskany, New York and Bridgewater, New Jersey

REPORT NO. 2A-II-00-09-065 DATE: July 20, 2010

This report details the results of our audit of the Federal Employee Group Life Insurance Program (FEGLI) operations at Metropolitan Life Insurance Company (MetLife) in its Oriskany, New York, and Bridgewater, New Jersey offices. The audit covered claim benefit payments, administrative expenses, and cash management activities for fiscal years 2007 and 2008. We also reviewed MetLife’s Fraud and Abuse program policies and procedures. The audit identified $708,518 in undercharges to the FEGLI program. The audit also showed that FEGLI cash and investment funds were commingled with MetLife’s corporate cash and investment funds. Except for these findings, we determined that the Program was administered in accordance with Contract 17000-G (between OPM and MetLife) and the Federal regulations. Our audit issues are summarized below.

CLAIM PAYMENTS

Our review of the benefit payments paid by MetLife on behalf of FEGLI participants showed that the benefits were paid in accordance with Contract 17000-G as well as the applicable Federal regulations.

FRAUD AND ABUSE PREVENTION AND DETECTION

Our review showed that MetLife had adequate policies and procedures in place to deter or detect incidence of insurance fraud and abuse in the FEGLI Program.
ADMINISTRATIVE EXPENSES

Pension Expense
• Our audit showed that the FEGLI was undercharged a total of $98,646 for pension expense in fiscal years 2007 and 2008.

Information Technology Expense
• Our audit showed that the FEGLI was undercharged a total of $609,872 for information technology costs in fiscal year 2008.

CASH MANAGEMENT ACTIVITIES

Commingling of Funds
• We determined that MetLife commingled FEGLI cash and investment funds with its corporate cash and investment funds in fiscal years 2007 and 2008. However, this audit issue was resolved with MetLife’s transfer of all FEGLI investment funds from its corporate investment pool to a separate investment portfolio exclusively for the investment of FEGLI funds in fiscal year 2009.
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I. INTRODUCTION AND BACKGROUND

INTRODUCTION

This report details the results of our audit of the Federal Employee Group Life Insurance Program’s (FEGLI or Program) operations at the Metropolitan Life Insurance Company (MetLife) in Oriskany, New York and Bridgewater, New Jersey. The audit was performed by the Office of Personnel Management’s (OPM) Office of the Inspector General (OIG), as established by the Inspector General Act of 1978, as amended.

BACKGROUND

The FEGLI Program was created in 1954 by the Federal Employees’ Group Life Insurance Act (Public Law 83-598). OPM’s Retirement and Benefits Office (RBO) has overall responsibility for administering the Program, including the publication of program regulations and agency guidelines; and the receipt, payment, and investment of agency withholdings and contributions. The RBO contracts with MetLife to provide life insurance coverage to employees, annuitants, and their family members (Contract No. 17000-G). Employer agencies are responsible for enrolling, informing, and advising employees of program changes, determining eligibility, maintaining insurance records, withholding premiums from pay, remitting and reporting withholdings to OPM, and certifying salary and insurance coverage upon separation or death.

MetLife’s responsibilities under the contract are carried out by its Office of Federal Employees’ Group Life Insurance (OFEGLI), a separate unit of MetLife, which is located in Oriskany, New York. OFEGLI had been part of the National Accounts unit within MetLife’s Institutional Business segment. On July 14, 2009, MetLife announced the combination of its Institutional and Individual Businesses and its Auto & Home unit into a single U.S. Business organization. OFEGLI is supervised by MetLife’s Group Insurance Department with technical and administrative assistance provided by OPM and various other MetLife departments.

In September 2009, MetLife transferred its claims processing function for the FEGLI Program to its Oriskany, New York office. MetLife’s accounting and financial operations are handled in their Bridgewater, New Jersey office.

Compliance with laws and regulations applicable to the FEGLI Program is the responsibility of MetLife’s management. Also, management of MetLife is responsible for establishing and maintaining a system of internal controls.

Our previous audit of MetLife (Report Number 2A-II-00-07-017, dated December 15, 2008), covered claim payments for fiscal year 2006, claim overpayments, administrative expenses and cash management activities for fiscal years 2005 and 2006. All findings questioned in that report, with the exception of the commingling issue, were satisfactorily resolved prior to the beginning of the current audit. The commingling issue, which is again identified as an audit issue in this report, was resolved in fiscal year 2009, with the movement of FEGLI funds into a separate investment portfolio established exclusively for the FEGLI program.
II. OBJECTIVES, SCOPE, AND METHODOLOGY

OBJECTIVES

The objectives of our audit were to determine whether costs charged to the FEGLI Program and services provided to FEGLI Program subscribers were in accordance with the terms of Contract 17000-G and the Federal regulations. Specifically, our objectives were as follows:

Benefit Charges

- To determine whether MetLife complied with the contract provisions relative to benefit payments.
- To determine whether overpayment recoveries were returned promptly to the FEGLI Program. Also, to determine whether MetLife made diligent efforts to recover overpayments.

Administrative Expenses

- To determine if the administrative expenses charged to the FEGLI Program were actual, necessary, and reasonable expenses incurred in accordance with the terms of the contract and applicable regulations.

Cash Management

- To determine whether MetLife handled FEGLI Program funds in accordance with applicable laws and regulations concerning cash management in the FEGLI Program.

Fraud and Abuse Prevention and Detection

- To determine what policies and procedures MetLife has in place to prevent and detect fraud, waste and abuse related to the FEGLI Program (specifically life insurance claims).
- To review any instances of fraud, waste and abuse identified by MetLife and the corrective actions that were implemented.

SCOPE

We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our audit findings and conclusions based on the audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on the audit objectives.

We reviewed the FEGLI Program financial statements for fiscal years 2007 and 2008. During this period, benefit charges totaled approximately $4.9 billion and administrative expenses totaled $14.5 million. Specifically, we reviewed claim payments in fiscal year 2008. We also
reviewed claim overpayments, administrative expenses, and cash management activities for fiscal years 2007 and 2008. In addition, we reviewed MetLife's policies and procedures to deter or detect instances of fraud and abuse in the FEGLI Program.

In conducting the audit, we reviewed approximately $21,825,300 in claim payments made from October 1, 2007 through September 30, 2008, for proper adjudication. We also reviewed $4,346,315 in claim overpayments, $2,817,105 in administrative expenses, and $907,610,379 in cash management letter of credit (LOC) drawdowns for compliance with cash management policies and procedures.

We obtained an understanding of MetLife's internal control structure to help determine the nature, timing, and extent of our auditing procedures. This was determined to be the most effective approach to select areas of audit. For those areas selected, we primarily relied on substantive tests of transactions and not tests of controls. Based on our testing, we did not identify any significant matters involving MetLife's internal control structure and its operation. However, since our audit would not necessarily disclose all significant matters in the internal control structure, we do not express an opinion on MetLife's system of internal controls taken as a whole.

We also conducted tests to determine whether MetLife had complied with the contract, the applicable procurement regulations (i.e., Federal Acquisition Regulations and Federal Employees Group Life Insurance Federal Acquisition Regulations, as appropriate), and the laws and regulations governing the FEGLI Program. Exceptions noted in the areas reviewed are set forth in detail in the "Audit Findings and Recommendations" section of this audit report. With respect to the items not tested, nothing came to our attention that caused us to believe that MetLife had not complied, in all material respects, with those provisions.

In conducting our audit, we relied to varying degrees on computer-generated data provided by MetLife. Due to time constraints, we did not verify the reliability of the data generated by MetLife's information systems. However, while utilizing the computer-generated data during audit testing, nothing came to our attention to cause us to doubt its reliability. We believe that the data was sufficient to achieve the audit objectives.

The audit was performed at MetLife's offices in Oriskany, New York from September 14, 2009 through September 25, 2009, and Bridgewater, New Jersey from October 19, 2009 through October 30, 2009.

**METHODOLOGY**

To test MetLife's compliance with the Contract provisions relative to claims payments, we judgmentally selected:

- 100 claim payments from the four highest dollar claim months in fiscal year 2008. Specifically, we reviewed the 25 highest claims from the months of December 2007, and March, June and September of 2008. Our judgmental sample of 100 claims represented $21,825,300 in claim payments out of a universe of 98,225 claims totaling $2,462,559,367. We traced the claims through the claims processing system,
reviewed MetLife's case files to determine if the necessary documents were provided, and verified whether the claim payments were correctly calculated and paid to the beneficiary.

To review MetLife's adjudication of its claim overpayment process to determine if overpayments were properly returned to the FEGLI Program, we judgmentally selected:

- All fiscal year 2007 and 2008 recoveries that were equal to or greater than $24,000, which totaled a sample of 50 overpayment recoveries (30 recoveries from fiscal year 2008 and 20 recoveries from fiscal year 2007). The 50 overpayment recoveries represented $4,346,315 out of a total of universe 763 recoveries totaling $5,206,607 returned in fiscal years 2007 and 2008.

To determine if administrative expenses were actual, necessary, and reasonable, we selected the following samples:

- From the three cost centers representing direct administrative expenses, we selected 16 out of 119 natural accounts for potential review. Natural accounts are expense accounts (i.e., salaries, rent, utilities, postage, etc.) that support the FEGLI cost centers. The 16 accounts were selected based on the highest activity per quarter in fiscal year 2008. The total amount sampled represented $1,436,999 out of a universe totaling $5,365,135. We also reviewed each account description to ensure only allowable costs were charged to the account.

- From the one cost center representing indirect administrative expenses, we selected 9 out of 10 natural accounts for potential review. The nine accounts selected represented the highest dollar amounts charged to the FEGLI program in fiscal year 2008. We sampled expenses of $1,380,106 out of a universe totaling $1,463,673. We also reviewed each account description to ensure only allowable costs were charged to the account.

- From the three cost centers representing direct administrative expenses, we also judgmentally selected an additional six natural accounts based on the highest expense accounts per quarter in fiscal year 2008. From the six natural accounts, we judgmentally selected 18 out of 115 transactions for a detailed review of the supporting invoices, based on the highest transaction amounts. The total amount sampled represented $63,979 out of a universe totaling $192,255.

- From a total of 27 administrative expense adjustments in fiscal year 2008, we selected 11 adjustment transactions based on high dollar transactions or transactions of unusual activity. The total amount sampled represented an absolute value of $48,017 out of a universe representing an absolute value of $227,193.

To determine whether MetLife handled FEGLI Program funds in accordance with the contract and applicable laws and regulations concerning recurring premium payments to carriers we:
• Judgmentally selected four months (two months from each fiscal year) based on the highest LOC monthly drawdowns. As a result, our sample included the daily drawdowns for the months of March and August (fiscal year 2007), and October 2007 and July 2008 (fiscal year 2008). The four month drawdown sample represented $907,610,379 of the total of $4,854,366,286 in LOC drawdown transactions occurring during fiscal years 2007 and 2008.

• Reviewed MetLife's policies and procedures for investing FEGLI Program funds to determine if MetLife was in compliance with the Contract and applicable Federal regulations regarding the commingling of federal funds.

To determine what fraud and abuse policies and procedures MetLife had in place to deter or detect instances of fraud and abuse in the FEGLI Program, and what corrective action was taken by MetLife for any instances that were identified, we:

• Reviewed MetLife's policies and procedures and interviewed a senior investigator from MetLife's Special Investigations Unit involved in investigating allegations of fraud and abuse in the FEGLI Program.

• Reviewed all open cases covering fiscal years 2007 through 2009 to determine if all amounts recovered were properly returned to the FEGLI Program.

The samples above that were selected and reviewed were not statistically based. Consequently, the results could not be projected to the universe since it is unlikely that the results are representative of the universe as a whole. We used the FEGLI Program contract; the Federal Acquisition Regulations; and the Federal Employees Group Life Insurance Federal Acquisition Regulations to determine the allowability, allocability, and reasonableness of the administrative expenses charged against the contract.

A draft report, dated January 14, 2009, was provided to MetLife for review and comment. MetLife's comments on the draft report were considered in preparing the final report and are included as an Appendix to this report.
III. AUDIT FINDINGS AND RECOMMENDATIONS

A. CLAIM PAYMENTS

Our review of the benefit payments paid by MetLife on behalf of FEGLI participants showed that the benefits were paid in accordance with Contract 17000-G as well as the applicable Federal regulations.

B. FRAUD AND ABUSE PREVENTION AND DETECTION

Our review of the fraud and abuse program implemented by MetLife showed that MetLife had adequate policies and procedures in place to deter or detect incidences of insurance fraud and abuse in the FEGLI Program.

C. ADMINISTRATIVE EXPENSES

1. Pension Expense ($98,646)

MetLife did not calculate pension costs in accordance with the Federal regulations for fiscal years 2007 and 2008. As a result, the FEGLI Program was undercharged $98,646 for pension costs.

48 CFR 31.205-6(j)(2) states that the cost of all defined-benefit pension plans shall be measured, allocated and accounted for in compliance with the provisions of 48 CFR 9904.412 and 48 CFR 9904.413. Pension costs are allowable subject to the referenced standards and the cost limitations and exclusions. The regulations limit the amount of pension costs that may be charged to a government contract to the lower of:

- the amount of any cash contribution to the pension fund trustee, or
- the amount of expense calculated in accordance with CAS 412 and 413, whichever is lower.

We found that MetLife did not calculate the pension costs based on the lesser of cash contributions (funded amount) or the CAS amount in fiscal years 2007 and 2008. We recalculated these costs by multiplying the lesser of the funded or CAS amount by the FEGLI’s corporate allocation percentage. As a result, MetLife’s pension costs were understated by $97,846 in 2007 and $800 in 2008. MetLife’s total undercharge to the FEGLI Program was $98,646.

MetLife Comments:

MetLife agrees with this finding and stated that it has documented its procedures for calculating the pension cost and included review and approval requirements to ensure that the pension expenses charged to the program are in compliance with the Federal Regulations.
**Recommendation 1**

We recommend that the contracting officer allow MetLife to collect $98,646 through the LOC drawdown account for pension expense undercharged in fiscal years 2007 and 2008.

**Recommendation 2**

We recommend that the contracting officer ensure that MetLife implements its procedures to ensure that the FEGLI pension expense is calculated in accordance with the Federal Regulations.

2. **Information Technology Expense**

MetLife undercharged the FEGLI program for its information technology (IT) services in fiscal year 2008. MetLife changed its internal processes which resulted in the Program’s IT costs being allocated to MetLife’s other lines of business. As a result, the FEGLI Program was undercharged a total of $609,872 for the IT services provided by MetLife in fiscal year 2008.

During our audit, we requested support for a judgmental sample of fiscal year 2008 administrative expenses, of which we included selected information technology expenses. While MetLife was researching the documentation to support these IT expenses they discovered that they had undercharged FEGLI for their information technology cost. This issue was not addressed in our draft report, as it was brought to our attention by MetLife subsequent to the issuance of the draft report.

**MetLife Comments:**

MetLife stated that it has a dedicated IT Application Development team that works on maintaining and updating the FEGLI claims system. MetLife captures these programming costs in dedicated client codes which are attributable to the FEGLI Program.

However, during fiscal year 2008, MetLife made changes to the internal process it uses to charge IT costs to its business areas. The changes inadvertently caused some of the FEGLI IT costs to be erroneously charged to other MetLife business areas. Because of this programming error, FEGLI was undercharged $560,048 for IT Application Development costs, and undercharged $49,825 for FEGLI System Infrastructure cost. MetLife requested to be reimbursed for total IT cost undercharges of $609,872. MetLife provided supporting documentation to the OIG for review.

**OIG Comment:**

We reviewed the documentation provided by MetLife and agree that the FEGLI Program was undercharged $609,872 for its IT costs in fiscal year 2008.
Recommendation 3

We recommend that the contracting officer allow MetLife to collect $609,872 through the local drawdown account for IT expense undercharged in fiscal year 2008.

Recommendation 4

We recommend that the contracting officer require MetLife to implement procedures to evaluate the impact of MetLife corporate policy and procedural changes on the FEGLI Program to ensure the administrative cost associated with the Program are accurately captured and charged to the FEGLI Program.

D. CASH MANAGEMENT ACTIVITIES

1. Commingling of Funds

MetLife commingled FEGLI cash and investment funds with MetLife corporate cash and investment funds during fiscal years 2007 and 2008. As a result, these FEGLI assets were not separately identifiable from other assets controlled by MetLife.

According to 48 CFR 2152.232-71, a contractor must maintain FEGLI Program funds in such a manner as to be separately identifiable from other assets of the contractor. However, if accounting techniques have been established to clearly measure FEGLI cash and investments, the regulations provide that a contractor can request the contracting officer to approve a modification of this provision.

MetLife’s investment objective is to provide liquidity and generate income while minimizing the erosion of the principal. MetLife’s FEGLI investments generally mature within a year and are maintained in a money market pool that is not specific to FEGLI. In fiscal years 2007 and 2008, income from the investments represents allocations from MetLife’s general account based on FEGLI’s proportionate investment contribution balance for each investment year. The allocated amounts did not represent separately identifiable assets as called for in the FEGLI regulations. In addition, FEGLI cash was in a commingled MetLife investment pool.

As stated in our prior audit, OPM informed MetLife (in a letter dated April 12, 1996) that it concurred with its practice of investing FEGLI monies in an investment pool with other MetLife funds. OPM stated that it did not intend to preclude the procedures MetLife used to invest FEGLI funds and that the allocation of investment income appeared reasonable and equitable.

However, although the OIG agrees that pooling of FEGLI funds with other lines of business may garner greater investment gains it also carries a greater risk for potential loss of FEGLI funds and accountability issues because of the commingling of FEGLI funds with other lines of business.
We reported on this issue in our prior audit report of the FEGLI operations at MetLife for fiscal years 2005 and 2006, dated December 15, 2008, and recommended that MetLife take steps to change its procedures to ensure FEGLI funds were not commingled with the MetLife investment pool. In response to our recommendation MetLife agreed to review its management of FEGLI assets.

As a result of our prior audit recommendations and changes in the economic environment in 2008, MetLife closed out all FEGLI’s investments in MetLife’s pooled investment portfolio (i.e., Woodstock) on December 16, 2008 (fiscal year 2009), and transferred these funds to a separate investment portfolio established exclusively for the investment of FEGLI funds.

Since this finding was resolved in fiscal year 2009 with the establishment of a separate FEGLI investment portfolio, the OIG is not offering a recommendation for this finding.
IV. MAJOR CONTRIBUTORS TO THIS REPORT

Special Audits Group

[Redacted] Auditor-In-Charge

[Redacted] Auditor

[Redacted] Chief [Redacted]
# Schedule A

**METROPOLITAN LIFE INSURANCE COMPANY**  
**ORISKANY, NEW YORK AND BRIDGEWATER, NEW JERSEY**  
**REPORT # 2A-II-00-09-065**  
Schedule of Contract Charges and Questioned Costs

## Contract Charges

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<td><strong>$2,426,901,963</strong></td>
<td><strong>$2,497,647,252</strong></td>
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## Questioned Charges

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<td>A. CLAIM PAYMENTS</td>
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<td>B ADMINISTRATIVE EXPENSES</td>
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<tr>
<td>1) Pension Expense</td>
<td>($97,846)</td>
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<tr>
<td>2) Information Technology Services</td>
<td>($609,872)</td>
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<tr>
<td>C. CASH MANAGEMENT ACTIVITIES</td>
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<tr>
<td>Procedual</td>
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<td>TOTAL QUESTIONED CHARGES</td>
<td>($97,846)</td>
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February 12, 2010

Office of Personnel Management
Office of the Inspector General
1900 E Street NW, Room 6400
Washington, DC 20415

Re: FEGLI Draft Audit Report

Dear [Name],

The following is our response to the draft FEGLI audit report dated January 14, 2010.

Administrative Expenses - Pension Expenses

Recommendation Number 1

We agree with this recommendation and look forward to the Contracting Officer’s determination.

Recommendation Number 2

We agree with Recommendation Number 2 and MetLife has documented its procedures to calculate pension costs according to 48 CFR 31.205 – 6 (j) (2). Included in the documentation is a requirement for review and signoff by MetLife management of the calculation of pension expenses charged to the program.

We can supply you with a copy of the procedures upon request.

Cash Management – Commingling of Funds

As stated in the draft report, this finding was resolved in fiscal year 2009.

MetLife identified the following item after the completion of the OIG’s field work and therefore it is not included in the referenced draft audit report:

MetLife has recently determined that the FEGLI Program was undercharged $609,872 in Information Technology (IT) costs during fiscal year 2008.
The following will briefly describe how this undercharge occurred.

MetLife has a dedicated IT Application Development team that works on maintaining and updating the FEGLI claim system. We capture these programming costs in dedicated client codes which are attributable to the FEGLI Program.

During fiscal year 2008, MetLife made changes to the internal process it uses to charge IT costs to its business areas. These changes inadvertently resulted in $560,048 of FEGLI IT costs accumulated to the FEGLI client code being allocated to other MetLife business areas.

In addition, this change also resulted in $49,825 of FEGLI System Infrastructure costs to be allocated to other business areas.

Attached for your review is a more detailed explanation of this undercharge as well as documentation for FEGLI’s IT expenses for the full fiscal year 2008.

We are requesting that MetLife be reimbursed $609,872 for these expenses.

If you have any question, please let me know.

Sincerely,

[Name]

Director

Cc: [Names]
MetLife has recently determined that the FEGLI Program was undercharged $609,872 in Information Technology (IT) costs during fiscal year 2008.

The following will describe how this undercharge occurred.

FEGLI’s IT costs generally consists of Application Development (AD) costs and Infrastructure costs.

**Direct Application Development (AD) Costs**
AD costs represent IT project work done by a staff of IT programmers on FEGLI system enhancements, time spent to meet regulatory and SOX requirements, maintenance, and support for the FEGLI Claim system. The IT programmers log in their time spent on the FEGLI Program using FEGLI specific IT project codes. Costs charged to these project codes are aggregated to client codes and then charged to the FEGLI Program.

During fiscal year 2008, MetLife made a change to its internal process that inadvertently caused costs for FEGLI system work captured in the FEGLI to be mapped to other business areas.

As a result of this change, the FEGLI Program was charged $130,451 for AD work while it incurred $690,499 in costs, an undercharge of $560,048.

**Infrastructure Costs**
Infrastructure costs represent charges for the FEGLI claim system’s dedicated servers, employee support, hardware, software and electricity. The costs are allocated based on the number of CPUs (central processing unit) of process bandwidth the FEGLI Claims system application uses.

During fiscal year 2008, MetLife changed the methodology to charge infrastructure related costs to their business areas. This change caused FEGLI’s infrastructure costs to be inadvertently mapped to other business areas. Therefore, the FEGLI Program was charged $190,027 for infrastructure costs in fiscal year 2008 while it incurred $239,852, undercharge of $49,825.
The following is a summary of costs charged to the program compared to costs incurred.

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<th>Federal Employees' Group Life Insurance</th>
<th>ITS</th>
<th>FY 2008</th>
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<td>53762 ISB-IT AMORTIZATION</td>
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<td>53868 CS IT FEGLI</td>
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<td>53883 CS IT Infrastructure 128,314</td>
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<td>IT Charged to the PROGRAM</td>
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<td>Application Development</td>
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<td>690,499</td>
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<td>Infrastructure</td>
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<td>239,852</td>
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<tr>
<td>Amortization</td>
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<tr>
<td>IT Incurred by the PROGRAM</td>
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<td>930,596</td>
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<tr>
<td>Application Development</td>
<td></td>
<td>(560,048)</td>
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<tr>
<td>Infrastructure</td>
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<td>(49,825)</td>
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<tr>
<td>(Undercharge) to the Program</td>
<td></td>
<td>$(609,872)</td>
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