

Defense Department Audit Report Card 2021



Defense Department Audit Report Card



In December 2020, the Defense Department (DoD) issued its latest annual Agency Financial Report. The financial statements in this report were a part of the third consecutive full-scope, department-wide audit. The COVID pandemic posed some special challenges and issues for the latest audit. The process took longer than in the previous year, but when all was said and done, the DoD received another disclaimer (failing) audit opinion on its financial statements.

Upon reviewing the massive set of documents relating to the audits for DoD and its component entities, we found significant continuing concerns regarding spending in one of the largest agencies in our federal government. The number of disclaimer opinions and identified material weaknesses remain high, but hopefully the component entities and their auditors are on a learning curve that will lead to better results in years to come.

With this report, Truth in Accounting ranks DoD component entities based on their fiscal year (FY) 2020 audit performance. We issue this ranking to identify relative strengths and weaknesses in financial reporting, to track progress over time, and to identify agency leaders who serve as good examples for the department as a whole.

Background

In 1990, the Chief Financial Officers Act directed federal agencies (including the DoD) to prepare and present audited financial statements, unless the agency asserted that its statements were not auditable. Such was the case for the DoD for nearly 30 years, at least until FY 2018.

This helps explain why the DoD has long been the principal culprit responsible for two decades

of annual disclaimer (failing) opinions on the consolidated financial statements for the entire United States Government.

In the latest year, auditors identified 26 material weaknesses in DoD agency-wide practices, up from 25 the previous year and 20 in FY 2018. This finding is both good and bad as more identified weaknesses can also represent progress in identifying opportunities for improvement. Below the agency-wide level, some entities were able to erase material weaknesses from previous years and progress continued on addressing and closing out previous years' auditor recommendations. However, the auditors continue to identify more new issues than the number that are resolved.

As in previous years, the DoD Inspector General recently issued a helpful report titled "[Understanding the Results of the Audit of the DoD FY 2020 Financial Statements](#)." Based on that report and our own analysis of the audit opinions for the DoD component entities, we have developed the scoring and ranking system described in the appendix.

Findings

The scores and ranking for the component entities are listed in the table on page five of this report. They are ranked from highest (best) to lowest (worst).

Based on our review, we recognize these five entities for delivering the best performance in the latest audit:

- **Defense Health Agency -- CRM**
- **Defense Contract Audit Agency**
- **Defense Finance and Accounting Service**
- **U.S. Army Corps of Engineers**
- **Military Retirement Fund**

Other DoD entities can learn from their example and improve their auditability in the years ahead.

Note that the main military branches—the Army, Navy, Air Force, and Marines—all rank at the bottom of the table. They are also among the largest entities, which poses significant financial management challenges. But we believe good accounting systems are even more important for the large military branches and we challenge them to rise in the rankings in the years ahead.

The DoD Inspector General's report "Understanding the Results of the Audit of the DoD FY 2020 Financial Statements" does not include the Department of Veteran Affairs (VA). We include the VA in our analysis because defense spending is much larger than just Defense Department expenses. The U.S. government spends massive defense-related dollars in other departments, including the VA, the Energy Department, the State Department, the Department of Homeland Security, and the Department of the Interior. We believe the VA, at least, belongs in a consolidated audit of "defense" financial reporting.

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Best-Performing DoD Entities



Defense Health Agency - Contract Resource Management

The DHA-CRM supports and coordinates health care services delivery to members of the Army, Navy and Air Force. It provides leadership for the DoD in achieving greater integration and efficiency in clinical and business processes for the Military Health System.

The DHA's Contract Resource Management arm (DHA-CRM) provides budget consultation, budget execution and contract and financial statement preparation services. The DHA-CRM 2020 agency financial report [is available here.](#)

Defense Contract Audit Agency (DCAA)

The DCAA reviews and audits contracts the DoD enters into with external suppliers, with a view to monitoring and managing costs of major weapons systems and outsourced services. The DCAA operates under the authority of the DoD Comptroller/CFO.

For anyone concerned about the cost and accountability of the overall DoD, at a minimum, it may be comforting to note that at least this critical agency performs well in terms of its own auditability. The DCAA's own financial statements and independent auditor's report for 2020 [are available here.](#)

Defense Finance and Accounting Service (DFAS)

The Defense Finance and Accounting Service (DFAS) provides specialized services to the rest of the Defense Department, including payroll processing and related human resource services for active and retired personnel, as well as payment services for Defense Department vendors.

The DFAS has included "Audit Steadiness" among the four "pillars" of its strategic plan, and it appears to have walked the talk on this score. DFAS has received unmodified (clean) audit opinions for 21 consecutive years.

The U.S. Army Corps of Engineers – Civil Works Program

The U.S. Army Corps of Engineers provides engineering, design and construction management services to the armed forces as well as a broader range of public projects. The Civil Works Program (USACE-CW) provides project development and maintenance services for water resource and navigation management projects, including locks and dams, and also builds and manages flood control systems.

The USACE-CW was one of a few Defense Department agencies to assert it was ready for audit in the years before the first DoD-wide audit. And it proved that it was indeed audit-ready, earning an unmodified (clean) audit opinion for the 11th consecutive year. The USACE-CW agency financial report for 2020 [is available here.](#)

Military Retirement Fund

The Military Retirement Fund (MRF) accumulates funds to finance the DoD's liabilities for military retirement and survivor benefit programs. The MRF is a defined benefit plan, with annual retirement payments totaling about \$40 billion for more than 1.5 million retirees.

Clean opinions and ranking well on our audit scores aren't necessarily a sign of financial strength, however. The MRF reported nearly \$1 trillion in total investment assets in 2020, but also reported \$1.8 trillion in liabilities, leaving a negative net position of more than \$800 billion.

The MRF's 2020 agency financial report [is available here.](#)



Criteria and Scoring



We base our score on eight criteria. The **OPINION** criterion is weighted at 30 percent. The **ACCESS**, **NFRs**, **dNFRs**, **MATERIAL WEAKNESSES**, **NON-COMPLIANCE**, **dMW/dNC** and **TIME** criteria are each weighted at 10 percent.

OPINION

This is the audit opinion. An unmodified (clean) opinion means the auditor deemed the statements were fairly presented and consistent with generally accepted accounting principles (GAAP). A clean opinion receives five points in our framework. A qualified opinion means the statements are presented fairly and consistent with GAAP, with noted material exceptions. A qualified opinion receives three points. The auditor delivers a disclaimer of opinion if it determines it cannot obtain sufficient evidence to render an opinion. A disclaimer of opinion receives one point. An adverse opinion earns zero points.

ACCESS

This is based on the ease of finding the entity's annual financial report and audit opinion from the home page of the entity's website. We rank the 18 entities on their results for these elements, and then assign them scores of one (worst) to five (best) for the "Access" criteria.

NFRs

This is based on the number of Notices of Findings and Recommendations (NFRs). Auditors issue NFRs to identify specific weaknesses in business practices and information processing controls. The 18 component entities are ranked from top to bottom on the number of NFRs, and then assigned scores of one through five based on the number of NFRs.

dNFRs

This is based on the change in the number of Notices of Findings and Recommendations from the previous year. The number of NFRs can go down as entities address previous auditor recommendations, but it can also go up as auditors find new issues.

MW

This is based on the number of identified material weaknesses. Material weaknesses are defined in federal audits as "deficiencies in internal control over financial reporting that result in a reasonable possibility that management will not prevent, or detect and correct, a material misstatement in its financial statements in a timely manner." The 18 component entities are ranked from top to bottom for the number of material weaknesses, and then assigned scores of one through five based on the number of material weaknesses.

NC

This is based on the number of identified instances of noncompliance with laws and regulations. The 18 component entities are ranked from top to bottom for the number of instances of noncompliance, and then assigned scores of one through five based on the number of instances of noncompliance.

dMW / dNC

This is the change in the number of instances of identified material weaknesses and noncompliance (positive or negative) from the previous year. The 18 component entities are ranked from top to bottom for the change in the number of instances of noncompliance, and assigned scores from one through five.

TIME

This is based on the number of days after the end of the fiscal year that the auditor's letter is dated.



Ranking of DoD Component Entities



Overall		OPINION	ACCESS	NFRs	dNFRs	MW	NC	dMW / dNC	TIME
4.5	Defense Health Agency -- CRM	5	5	4	5	5	5	3	3
4.4	Defense Contract Audit Agency	5	1	5	5	5	5	3	5
4.3	Defense Finance and Accounting Service	5	1	5	5	5	5	3	4
4.1	U.S. Army Corps of Engineers	5	5	3	5	4	3	3	3
4.1	Military Retirement Fund	5	1	4	5	5	5	3	3
4	Defense Commissary Agency	5	5	4	1	4	4	3	4
3.7	DOD IG	5	5	4	2	3	2	5	1
3.6	Department of Veteran Affairs	5	5	3	5	3	1	3	1
3.3	Medicare-Eligible Retiree Health Care Fund	3	1	4	5	4	4	3	3
2.7	US Transportation Command	1	5	2	3	3	3	5	3
2.2	US Special Operations Command	1	1	2	4	3	3	3	3
2	Defense Health Program	1	5	2	4	1	1	1	3
1.9	Defense Information Systems Agency	1	1	3	1	3	2	3	3
1.8	Defense Logistics Agency	1	1	1	3	2	3	3	2
1.7	U.S. Army	1	1	1	2	1	3	3	3
1.7	U.S. Marine Corps	1	1	2	4	2	1	1	3
1.6	U.S. Air Force	1	1	1	2	1	3	3	2
1.5	U.S. Navy	1	1	1	2	1	3	3	1

Each entity is scored based on ten criteria: the auditor's **opinion**, the ease of **access**, the number of **NFRs**, the number of **NFRs-reissued**, the number of **NFRs-closed**, the number of **material weaknesses**, the **change in material weaknesses**, the number of noncompliance instances, the **change in noncompliance instances**, and the amount of **time** after the fiscal year-end the report was published. Please see page four for a breakdown of the scoring criteria.

