



DoD INSTRUCTION 7600.06

AUDIT OF NONAPPROPRIATED FUND INSTRUMENTALITIES AND RELATED ACTIVITIES

Originating Component: Office of the Inspector General of the Department of Defense

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Approved by: Sean O'Donnell, Acting Inspector General of the Department of Defense

Purpose: In accordance with the authority in DoD Directive 5106.01, this issuance establishes policy, assigns responsibilities, and prescribes procedures for audits of nonappropriated fund instrumentalities (NAFI) and related activities.

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SECTION 1: GENERAL ISSUANCE INFORMATION

1.1. APPLICABILITY.

This issuance applies to OSD, the Military Departments, the Office of the Chairman of the Joint Chiefs of Staff and the Joint Staff, the Combatant Commands, the Office of Inspector General of the Department of Defense (IG DoD), the Defense Agencies, the DoD Field Activities, and all other organizational entities within the DoD (referred to collectively in this issuance as the “DoD Components”).

1.2. POLICY.

a. In accordance with DoD Instruction (DoDI) 1015.15, annual audits will be conducted for all NAFIs with annual revenues or expenses exceeding \$10 million.

(1) For the purposes of this issuance, annual revenues or expenses must include resources recorded in the nonappropriated fund (NAF) financial records. This includes appropriations provided to a NAFI under a memorandum of agreement and treated and expended as NAF following the procedures established in DoDI 1015.15.

(2) To maintain the integrity of financial records, annual financial audits must be conducted, regardless of the dollar threshold of revenues and expenses, for NAFIs in Program Group VI – Special Purpose Central Funds and NAFIs supporting operations deemed to be highly sensitive.

b. Unless supported by appropriated funds or personnel in accordance with Paragraph 3.3, NAFIs will contract with a licensed independent certified public accountant (CPA) firm to satisfy the financial statement audit requirement, in accordance with DoDI 1015.15. These audits will include the headquarters, intermediate-level, and individual NAFIs as necessary for auditors to express an opinion on the NAFI financial statements of the Military Services. A financial statement audit is required annually. DoD personnel, rather than CPA firms, must be used for audits involving potential fraud or other serious improprieties.

c. NAF accounting systems must comply with generally accepted accounting principles in accordance with accounting standards established by the Financial Accounting Standards Board. NAF accounting systems must comply with the uniform chart of accounts established in Volume 13 of DoD 7000.14-R, except the Military Services exchanges, which maintain a uniform chart of accounts in accordance with DoDI 1015.15.

d. Results from audits will be made available directly to the audited entity in the form of a report in accordance with Government Auditing Standards.

e. All audits will be accomplished in accordance with the requirements of DoDI 7600.02 and Government Auditing Standards. Internal audits must meet the requirements in DoDI 7600.02 and this issuance.

f. The establishment, management, and control of NAFIs and the financial management of supporting resources must be accomplished in accordance with DoDI 1015.15.

SECTION 2: RESPONSIBILITIES

2.1. IG DOD.

The IG DoD establishes and monitors adherence to standards, policies, and procedures for the performance of DoD audits in accordance with DoD Directive 5106.01 and the Inspector General Act of 1978, as amended, in the Appendix of Title 5, United States Code.

2.2. DIRECTOR, DEFENSE CONTRACT AUDIT AGENCY.

Under the authority, direction, and control of the Under Secretary of Defense (Comptroller)/Chief Financial Officer, Department of Defense, the Director, Defense Contract Audit Agency:

- a. Upon request, provides reimbursable audit services for evaluations of price proposals for negotiated contracts exceeding \$2 million and costs incurred under cost reimbursement or incentive-type contracts.
- b. On a limited basis, performs reimbursable reviews of contracts that include clauses guaranteeing that prices will not exceed those offered to other customers.

2.3. SECRETARIES OF THE MILITARY DEPARTMENTS.

The Secretaries of the Military Departments:

- a. Prescribe procedures to provide adequate audit coverage of NAFIs, in accordance with DoDI 7600.02.
- b. Require that adequate audit coverage is provided for NAFIs.
- c. Issue guidance that requires audit reports to be directed to the appropriate management level with the authority and responsibility to ensure corrective action is taken on the findings and recommendations.
- d. Require that follow-up and resolution of audit recommendations are accomplished in accordance with DoDI 7650.03.
- e. Authorize staffing to conduct NAFI audits when the magnitude of operations, an internal review, or a local audit justifies it is deemed necessary.
- f. Establish a committee made up of senior officials, independent of NAFI management, to oversee its NAFI audits. The committee will establish audit requirements, which will include performance audits and attestation engagements. The requirements will be based upon risk assessments, contract deliverables, and the CPA firm's contract for the financial statement audit.

g. Analyze audits of NAFIs and prepare advisory or trend reports to help NAFI managers improve internal controls and operations.

h. Through their Military Department audit organizations heads:

(1) Require that, during annual risk-based planning, NAFIs within their cognizance are provided adequate audit coverage.

(2) Assist management to determine the frequency and scope of audit coverage for the individual NAFIs.

(3) Serve as advisors to the audit committee but are not voting members.

(4) Audit and review NAFIs based on risk assessment criteria, when appropriate.

(5) Provide technical guidance and periodically review audits conducted by NAFI internal audit staffs and CPAs that ensure such audits conform with DoDI 7600.02 and Government Auditing Standards.

SECTION 3: PROCEDURES

3.1. TYPES AND OBJECTIVES OF NAFI AUDITS.

a. Financial audits provide an opinion on whether the financial position of the NAFIs and the results of operations and cash flows are presented fairly, when applicable, in accordance with generally accepted accounting principles listed at <https://www.fasb.org> and DoD policy. An example is the audit contracted with a licensed independent CPA firm to satisfy the financial statement audit requirement, as established in Government Auditing Standards. Other types of financial audits can include auditing compliance with applicable requirements relating to NAFI programs.

b. Performance audits determine whether desired NAFI program results are achieved and resources are protected and managed economically and efficiently. Performance audit objectives vary widely. For example, performance audit objectives include determining whether:

(1) NAFI internal control systems are adequate and effective, and whether fees assessed cover costs.

(2) Applicable laws, regulations, and established NAFI policies and procedures are followed.

c. Attestation engagements report on a subject matter or an assertion about a subject matter that is the responsibility of another party. The three types of attestation engagements are an examination, a review, or agreed-upon procedures. Attestation engagements can have a broad range of objectives, such as an examination of a NAFI's internal controls over financial reporting and a review of a NAFI's accuracy and reliability of reported performance measures.

3.2. FREQUENCY OF AUDIT COVERAGE AND RISK FACTORS.

a. Performance audits and attestation engagements will be completed as deemed necessary by the NAFI internal audit staff, CPA firms, Military Department audit agencies, or the IG DoD based on risk assessments and resource availability.

b. NAFIs must be evaluated to determine the frequency of audit coverage. In assessing the risk, the following factors must be considered:

(1) Susceptibility to fraud, waste, and abuse.

(2) Visibility and impact.

(3) Time elapsed since the last audit.

(4) Adequacy of internal control systems.

(5) Effectiveness of controls for information technology systems.

- (6) Materiality of annual revenues and expenses.
- (7) Extent and results of oversight coverage by other DoD organizations.
- (8) Results of prior audits.
- (9) Extent and adequacy of operating policies and procedures.

c. Groups of activities, including those operating as an entity, may be audited as a system or on a functional basis. For example, functions that can be audited are personnel management and NAF investments or treasury management. In such instances, a single audit report or appraisal may be prepared to present an opinion or evaluation of the overall operations of the system or function. The audit report or appraisal will be based on the results derived from the audits of the individual activities selected by the auditors as representative of the system or function. The results would be projected to an evaluation or conclusion on the effectiveness of the overall system or function or its appropriate elements.

(1) A system must include:

(a) A uniform accounting system in accordance with the DoD uniform chart of accounts.

(b) Adequate internal control procedures.

(c) Organizational controls.

(d) A consolidation of the reports of the accounting system into meaningful financial summaries for the group. Military Service operating management must use the combined reports as a basis for overall control and direction.

(2) An auditor who is planning to perform a NAFI audit must consider the functional weaknesses identified in vulnerability assessments and management control reviews under the requirements of DoDI 5010.40.

3.3. CONDUCTING AND FUNDING AUDITS.

a. Performance audits and attestation engagements may be completed using NAFI internal audit staffs or reimbursing Military Department audit organizations. Annual financial statement audits will be accomplished by contracting with independent CPA firms. NAF support of NAFI audits is the preferred method for funding the audit.

b. Appropriated funds or personnel may be used to support NAFI audits when considered necessary by the DoD Component head concerned, and when not prohibited by law or regulation.

c. The annual financial statement audit must include the central NAFIs (if maintained) and regional, installation, or base NAFIs as deemed necessary. This is required to obtain relevant,

accurate, and complete financial information for the NAFIs under the cognizance of the Military Departments.

d. Specific policies and responsibilities regarding audits of NAFI and Military Service exchange credit systems are contained in DoDI 1015.15 and DoDI 1330.21.

e. Specific policies and responsibilities regarding audits on civilian morale, welfare, and recreation NAFIs are contained in DoDI 1015.08.

f. Non-Federal entities, as defined by Paragraph 3.a of DoDI 1000.15, that operate on DoD installations, will not receive funds, appropriated or nonappropriated, or personnel support for auditing their operations. However, to protect the interest of the United States, DoD Component heads may authorize support for official inquiries into operations of private organizations on DoD installations. Non-Federal entities include:

- (1) Veterans organizations.
- (2) Parent-teacher associations.
- (3) Model clubs.
- (4) Thrift clubs.
- (5) Residential community associations.
- (6) State, interstate, Indian tribal, or local government.
- (7) Private organizations.

g. When groups of appropriated and nonappropriated fund activities are operating as an entity, such as the MWR program, non-reimbursable use of appropriated funds or personnel may be used unless prohibited by law or regulation.

GLOSSARY

G.1. ACRONYMS.

ACRONYM	MEANING
CPA	certified public accountant
DoDI	DoD instruction
IG DoD	Inspector General of the Department of Defense
NAF	nonappropriated fund
NAFI	nonappropriated fund instrumentalities

G.2. DEFINITIONS.

Unless otherwise noted, these terms and their definitions are for the purpose of this issuance.

TERM	DEFINITION
audit	Financial audits, attestation engagements, and performance audits conducted in accordance with Government Auditing Standards.
annual financial audits	Defined in Government Auditing Standards.
highly sensitive operation	Operations that are inclined to potential fraud, large public exposure, and a high degree of investment activity or other risks.
internal audit	A function that helps DoD management attain its goals by providing information, analyses, assessments, and recommendations relevant to DoD management duties and objectives. The internal audit function supports the DoD Component heads.
Military Department audit organizations	The Army Audit Agency, Naval Audit Service, and Air Force Audit Agency.
NAFI internal audit staffs	The Army and Air Force Exchange Service, Marine Corps Nonappropriated Fund Audit Service, and Navy Exchange Service Command.
performance audits and attestation engagements	Defined in Government Auditing Standards.

REFERENCES

- Comptroller General of the United States, “Government Auditing Standards,” current edition
- DoD 7000.14-R, Volume 13, “Department of Defense Financial Management Regulation (DoD FMR): Nonappropriated Funds Policy,” current edition
- DoD Directive 5106.01, “Inspector General of the Department of Defense (IG DoD),” April 20, 2012, as amended
- DoD Instruction 1000.15, “Procedures and Support for Non-Federal Entities Authorized to Operate on DoD Installations,” October 24, 2008
- DoD Instruction 1015.08, “DoD Civilian Employee Morale, Welfare, and Recreation (MWR) Activities and Supporting Nonappropriated Fund Instrumentalities (NAFI),” December 23, 2005
- DoD Instruction 1015.15, “Establishment, Management, and Control of Nonappropriated Fund Instrumentalities and Financial Management of Supporting Resources,” October 31, 2007, as amended
- DoD Instruction 1330.21, “Armed Services Exchange Regulations,” July 14, 2005
- DoD Instruction 5010.40, “Managers’ Internal Control Program Procedures,” May 30, 2013, as amended
- DoD Instruction 7600.02, “Audit Policies,” October 16, 2014, as amended
- DoD Instruction 7650.03, “Follow-up on Inspector General of the Department of Defense (IG DoD) and Internal Audit Reports,” January 31, 2019
- United States Code, Title 5, Appendix, Inspector General Act of 1978, as amended