

**QUALITY
CONTROL
REVIEW
REPORT**

**QUALITY CONTROL REVIEW OF KPMG LLP
AND DEFENSE CONTRACT AUDIT AGENCY
AUDIT OF SMITHSONIAN INSTITUTION FOR
FISCAL YEAR ENDED SEPTEMBER 30, 1999**

November 16, 2000



National Aeronautics and
Space Administration

OFFICE OF INSPECTOR GENERAL

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Acronyms

AICPA	American Institute of Certified Public Accountants
OMB	Office of Management and Budget
DCAA	Defense Contract Audit Agency
ONR	Office of Naval Research
SOP	Statement of Position

Office of Inspector General

November 16, 2000

Ms. Barbara Reilly, Regional Director
Mid-Atlantic Region
Defense Contract Audit Agency
615 Chestnut Street, Suite 1000
Philadelphia, PA 19106-4498

Re: Final Report on Quality Control Review of KPMG LLP and Defense Contract Audit Agency Audit of Smithsonian Institution for Fiscal Year Ended September 30, 1999
Assignment Number A0004900
Report Number IG-01-004

Dear Ms. Reilly:

The subject final report is provided for your use and comment. Please refer to the Executive Summary for the overall audit results. Our evaluation of your response is incorporated into the body of the report. Your comments on a draft of this report were responsive to the recommendations. Management's completed actions are sufficient to close the recommendations for reporting purposes.

If you have questions concerning the report, please contact Mr. Patrick A. Iler, Director, Audit Quality, at (216) 433-5408, or Ms. Vera J. Garrant, Auditor-in-Charge, at (202) 358-2596. We appreciate the courtesies extended to the audit staff. The final report distribution is in Appendix E.

Sincerely,

[original signed by]

Russell A. Rau

Enclosure

cc:

AO/Chief Information Officer

B/Chief Financial Officer

B/Comptroller

BF/Director, Financial Management Division

G/General Counsel

H/Associate Administrator for Procurement

JM/Acting Director, Management Assessment Division

Mr. Earl J. Newman, Jr., Assistant Director of Operations, Headquarters, Defense
Contract Audit Agency

Mr. Lawrence P. Uhlfelder, Assistant Director of Policy and Plans, Headquarters, Defense
Contract Audit Agency

Mr. Mark Moser, Branch Manager, Columbia Branch, Defense Contract Audit Agency

Mr. Richard T. McKinless, Partner, KPMG LLP

bcc:
AIGA, IG Chrons

Office of Inspector General

November 16, 2000

Mr. Richard T. McKinless, Partner
KPMG LLP
2001 M Street, NW
Washington, DC 20036

Re: Final Report on Quality Control Review of KPMG LLP and Defense Contract Audit
Agency Audit of Smithsonian Institution for Fiscal Year Ended September 30, 1999
Assignment Number A0004900
Report Number IG-01-004

Dear Mr. McKinless:

The subject final report is provided for your use and comment. Please refer to the Executive Summary for the overall audit results.

If you have questions concerning the report, please contact Mr. Patrick A. Iler, Director, Audit Quality, at (216) 433-5408, or Ms. Vera J. Garrant, Auditor-in-Charge, at (202) 358-2596. We appreciate the courtesies extended to the audit staff. The final report distribution is in Appendix E.

Sincerely,

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Mr. Mark Moser, Branch Manager, Columbia Branch, Defense Contract Audit Agency

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NASA Office of Inspector General

IG-00-004
A0004900

November 16, 2000

Quality Control Review of KPMG LLP and Defense Contract Audit Agency Audit of Smithsonian Institution Fiscal Year Ended September 30, 1999

Executive Summary

Background. The Smithsonian Institution (Smithsonian), Washington, D.C., is a museum, education, and research complex consisting of 16 museums and galleries, the National Zoological Park, and other research facilities. The Smithsonian's museums and facilities perform research throughout the world. All Federal awards to the Smithsonian are for research and development.

The National Aeronautics and Space Administration (NASA) is the cognizant agency for audit for the Smithsonian. The NASA Office of Inspector General performed a quality control review of the KPMG LLP (KPMG) and Defense Contract Audit Agency (DCAA) audit of the Smithsonian financial statement and research and development major program¹ for the fiscal year ended September 30, 1999.² The Single Audit Act and the Single Audit Act Amendments³ require the audits. The Smithsonian has separate accounting systems for the Mall-based entities⁴ and the Smithsonian Astrophysical Observatory. KPMG and DCAA coordinated the Office of Management and Budget (OMB) Circular A-133⁵ audit to include both accounting systems. The Smithsonian reported total fiscal year Federal expenditures for NASA of about \$52.4 million and total expenditures of \$66.3 million.

Appendix A provides details on the single audit requirements.

¹A major program is a Federal program that the auditors determined through a risk analysis is subject to audit for the organization's current fiscal year.

²The Washington, D.C., office of KPMG, and the Columbia Branch, Columbia, Maryland, office of DCAA, performed the single audit for the Smithsonian for the fiscal year ended September 30, 1999. KPMG and DCAA audited different components of the Smithsonian.

³OMB Circular A-133, "Audits of States, Local Governments, and Non-Profit Organizations," implements the requirements of the Single Audit Act and the Single Audit Act Amendments. Appendix A contains details on the requirements of the Circular.

⁴The Mall-based institutions are those located in downtown Washington, D.C.; for example, the museums and galleries, the National Zoological Park, and other research facilities.

⁵See footnote 3.

Objectives. The objective of our report review was to determine whether the audit report the Smithsonian submitted to the Federal Audit Clearinghouse⁶ meets applicable reporting standards and OMB Circular A-133 reporting requirements.

The objectives of our quality control review were to determine whether KPMG and DCAA conducted the audit in accordance with applicable standards and whether the audit meets the auditing and reporting requirements of OMB Circular A-133. See Appendixes B and C for details on the objectives, scope, and methodology.

Results of Review. The KPMG audit work meets the auditing requirements of OMB Circular A-133 and generally accepted government auditing standards (GAGAS).⁷ The DCAA audit work does not meet the auditing requirements of OMB Circular A-133 and GAGAS in several areas.

- **Reported A-133 Results.** KPMG issued its audit report on the Smithsonian on January 14, 2000. For the compliance requirements in its audit scope, KPMG (1) identified no findings, (2) questioned no costs, and (3) issued an unqualified opinion⁸ on the financial statements, Schedule of Expenditures of Federal Awards,⁹ and major program compliance.¹⁰ Also, the auditors found no instances of noncompliance in the financial statement audit that are required to be reported under GAGAS. Finally, the auditors noted no matters involving internal controls (relating to the financial statement or major programs) that are considered to be material weaknesses.¹¹

DCAA issued its audit reports on the Smithsonian and Smithsonian Astrophysical Observatory on June 27, 2000. For the compliance requirements in its audit scope, DCAA (1) identified findings, (2) questioned indirect costs, and (3) issued an unqualified opinion on the Schedule of Expenditures of Federal Awards and major program compliance. Also, the

⁶The Single Audit Act Amendments of 1996, §7504(c), require OMB to establish the Federal Audit Clearinghouse to receive audit reports prepared pursuant to Circular A-133.

⁷These standards are broad statements of the auditors' responsibilities promulgated by the Comptroller General of the United States.

⁸An unqualified opinion means that the financial statements are presented fairly in all material respects, expenditures of Federal funds are presented fairly, in relation to the financial statements taken as a whole, and the auditee has complied with all applicable laws, regulations, and contract provisions that could have a direct and material effect on each major program.

⁹The Schedule of Expenditures of Federal Awards shows the amount of annual Federal award expenditures by Federal agency for each program, grant, or contract.

¹⁰Major program compliance refers to an assessment of the auditee's compliance with laws, regulations, and provisions of contracts or grant agreements that could have a direct and material effect on each major program.

¹¹The American Institute of Certified Public Accountants Statement of Position 98-3, Appendix D, defines a material weakness as "... the condition in which the design or operation of one or more of the internal control components [control environment, risk assessment, control activities, information and communication, and monitoring] does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions."

auditors noted matters involving major program internal controls that are reportable conditions, but are not considered to be material weaknesses.

- **Report Quality Review Results.** The Smithsonian audit report meets the applicable reporting guidance and regulatory requirements in OMB Circular A-133.
- **Audit Quality Review Results.** The KPMG audit work meets the applicable auditing and reporting guidance and regulatory requirements in (1) OMB Circular A-133 and its related Compliance Supplement, (2) GAGAS, and (3) generally accepted auditing standards.

The DCAA audit work does not meet the applicable auditing and reporting guidance and regulatory requirements in (1) OMB Circular A-133 and its related Compliance Supplement, (2) GAGAS, and (3) generally accepted auditing standards. For the compliance requirements within its audit scope, DCAA auditors did not:

- adequately document the working papers for (1) their understanding of internal controls, (2) the compliance attributes tested to support their opinion, and (3) the audit sampling plan (Finding A) as required by GAGAS and generally accepted auditing standards;
- test internal controls (Finding B) as required by OMB Circular A-133; and
- audit the procurement compliance requirement (Finding C) as required by OMB Circular A-133.

Recommendations. We recommend that for the Smithsonian's fiscal year ended September 30, 1999, and for future audits, DCAA:

- Document its working papers with the auditors' understanding of internal controls, the attributes tested for each of the compliance requirements, and the audit sampling plan.
- Plan and conduct tests of internal controls.
- Perform the audit of the compliance requirement in accordance with OMB Circular A-133.

Management's Response. DCAA management partially concurred with all the recommendations. Management agreed with the intent of the recommendations, but did not agree that the audit report is unreliable because the auditors did not perform and document the work required for the audit. The DCAA auditors revised and supplemented the original audit working papers to meet the intent of the recommendations. In addition, management decided to provide training to all its auditors on general and OMB Circular A-133 working paper documentation.

Evaluation of Management's Response. We consider management's comments and completed corrective actions responsive to the intent of the recommendations. Therefore, the recommendations are dispositioned and closed.

Introduction

The Single Audit Act Amendments of 1996 (Public Law 104-156) and the June 24, 1997, revision to OMB Circular A-133 require that an auditee obtain an annual audit of its fiscal year Federal expenditures. The audit must be performed by independent auditors and must be in accordance with the Single Audit Act Amendments of 1996, OMB Circular A-133 and its related Compliance Supplement, and the GAGAS that are applicable to financial audits.

A complete reporting submission in accordance with OMB Circular A-133 includes the following: (1) financial statements and related opinion, (2) Schedule of Expenditures of Federal Awards and related opinion, (3) report on internal controls and compliance review on the financial statements, (4) report on internal controls review and compliance opinion on major programs, and a (5) Schedule of Findings and Questioned Costs.¹²

Appendix A contains additional details on the Single Audit requirements.

¹²Appendix C describes the information contained in the Schedule of Findings and Questioned Costs.

Findings and Recommendations

Finding A. Working Paper Documentation

The DCAA auditors did not document their working papers for (1) their understanding of internal controls, (2) the compliance attributes tested, and (3) the audit sampling plan. This occurred because the auditors relied on their past audit experience and on DCAA's historical method for assessing internal control at the organization level rather than at the compliance requirement level. As a result, Federal agencies and other report users cannot rely on the OMB Circular A-133 audit report related to the DCAA audit scope.

Working Paper Documentation Requirements

The American Institute of Certified Public Accountants (AICPA) Codification of Statements on Auditing Standards §339.05, "Content of Working Papers," and GAGAS, sections 4.34 through 4.37, "Working Papers," require auditors to retain a record of the audit in the form of working papers to demonstrate that the applicable standards of field work have been met. GAGAS further state that the form and content of the working papers should allow an experienced auditor to understand the auditor's significant conclusions and judgments. In general, the working papers should document the objectives, scope, and methodology, including the sampling criteria the auditors used. Specifically, working papers should include enough information about the work performed and the documents (transactions and records) examined so that an experienced auditor would be able to examine the same documents and understand the auditors' judgments and conclusions.

Internal Controls

OMB Circular A-133 §___.500 requires the auditor to perform an audit of the entire organization in accordance with GAGAS. The audit scope includes the financial statements, internal controls, and compliance over Federal programs. In general, §___.500(c)(1) requires the auditor to perform procedures to obtain an understanding of internal controls over Federal programs that is sufficient to plan the audit for major programs. The AICPA Statement of Position (SOP) 98-3, "Audits of States, Local Governments, and Not-for-Profit Organizations Receiving Federal Awards," sections 8.7, 8.10, and 8.16, describe the auditors' responsibilities for planning the review of internal controls for major programs. The auditors must obtain a sufficient understanding of internal control over Federal programs by performing procedures to understand the design of the five internal control components (control environment; risk assessment; control activities; information and communication; and monitoring) related to the A-133 compliance requirements¹³ for each major program.

¹³Appendix A lists the compliance requirements.

Division of Audit Responsibilities. The Smithsonian has separate accounting systems for the Mall-based entities¹⁴ and the Smithsonian Astrophysical Observatory. The DCAA and KPMG auditors divided the audit work (compliance testing and internal control) for the 14 compliance requirements¹⁵ of the Smithsonian and the Smithsonian Astrophysical Observatory into 3 categories: Mall-based, Smithsonian Astrophysical Observatory, and Smithsonian-wide. The DCAA auditors were responsible to audit the following requirements:

Identification of DCAA Audit Responsibilities

<u>Compliance Requirement</u>	<u>Area of Responsibility</u>
Activities Allowed or Unallowed (Direct expenses)	SAO* only
Activities Allowed or Unallowed (Indirect expenses)	Smithsonian-wide
Allowable Costs/Cost Principles (Direct expenses)	SAO only
Allowable Costs/Cost Principles (Indirect expenses)	Smithsonian-wide
Eligibility	SAO only
Equipment and Real Property Management	SAO only
Period of Availability of Federal Funds (Direct expenses)	SAO only
Period of Availability of Federal Funds (Indirect expenses)	Smithsonian-wide
Procurement and Suspension and Debarment	SAO only
Subrecipient Monitoring	SAO only
Special Tests and Provisions	SAO only

* Smithsonian Astrophysical Observatory

DCAA Working Paper Documentation. DCAA did not meet GAGAS and AICPA standards for working paper documentation. The DCAA auditors did not document their working papers for the five components of internal control for each of the compliance requirements in their audit scope. The auditors rely on the information that DCAA maintains in permanent files on specific accounting systems of the Smithsonian at the organization level. OMB Circular A-133 and its related Compliance Supplement require the auditor to document internal controls at the compliance requirement level for each major program. The DCAA working paper documentation consists of a series of yes/no checklists that do not require the auditors to provide further explanations to their responses. Some of the checklists are incomplete, and most of the responses do not refer to documentation that support the auditors’ responses. Some of the responses refer to the DCAA permanent file, but the permanent file contains only copies of the Smithsonian policies and procedures, handbooks, and sample form documents. The permanent files should contain a write-up of the auditors’ understanding of the five components of internal control for each of the compliance requirements. The auditors may

¹⁴See footnote 4.

¹⁵Appendix A describes the compliance requirements.

also include the internal control write-up in the audit working papers instead of the permanent file. Due to the lack of adequate internal control documentation, the only way a reviewer could understand the auditors' answers in the DCAA internal control checklist would be to read and analyze the entire DCAA permanent file.

Compliance Requirements

Planning Compliance Tests OMB Circular A-133 §__.505(c) requires the auditors to express an opinion on whether the audited organization complied with laws, regulations, and the provisions of contracts or grant agreements that may have a direct and material effect on each major program. AICPA SOP 98-3, sections 6.31, 6.33, and 6.35, state that during the planning process, the auditors should develop an overall audit strategy to determine the nature, timing, and extent of work necessary to accomplish the audit objectives. The auditors should plan the audit to use the understanding of the internal controls they obtained to (1) identify types of potential noncompliance, (2) consider factors affecting the risk of material noncompliance, and (3) design compliance tests.

Performing Compliance Testing OMB Circular A-133 §__.500(d)(1) and (4) and AICPA SOP 98-3, section 6.22, require the auditors to determine whether the Federal award recipient complied with the laws, regulations, and contract and grant provisions that materially affect the major program. Compliance testing includes transactions and other auditing procedures that provide the auditors with sufficient evidence to support an opinion on compliance. Part 3 of the Compliance Supplement provides the auditors guidance to review compliance for each of the 14 compliance requirements. This information is intended to assist the auditors to plan and perform tests to determine whether the auditee complied with the Federal program requirements. AICPA SOP 98-3, section 6.6, states that sufficient evidence to support compliance reduces audit risk¹⁶ to an appropriately low level. Sections 6.39, 6.36, and 6.37 state that the purpose of the compliance testing is for the auditors to apply procedures to provide reasonable assurance of detecting material noncompliance to determine whether the auditee materially complied with the compliance requirements.

DCAA Working Paper Documentation The DCAA audit working papers do not document the compliance attributes tested for each of the compliance requirements within its audit scope. The DCAA audit working papers include a summary of the work performed and supporting documentation for the expenditures tested. The summary working paper identifies the expenditures selected for compliance testing and the auditors' conclusion for each expenditure. The auditors included copies of purchase orders, vouchers, and other information that supports the charge to Federal awards. However, the auditors did not identify the specific attributes or criteria they used to determine whether the expenditure should be charged to Federal programs.

¹⁶ AICPA SOP 98-3, section 6.7, defines audit risk as the risk that “. . . the auditor may unknowingly fail to appropriately modify his or her opinion on compliance.”

For example, for the compliance requirement related to activities allowed or unallowed, the auditors did not state in the working papers that they ensured the charge was an acceptable activity under the award. The auditors have extensive knowledge about the Smithsonian from prior audit work, but they did not document the working papers accordingly for a reviewer to understand the auditors' conclusions and judgments.

Sampling Plan

The DCAA auditors did not create a sampling plan. Generally accepted government auditing standards, section 4.37(a), states: "Working papers should contain the objectives, scope, and methodology, including any sampling criteria used" The DCAA auditors did not create a sampling plan because they did not know they needed one for judgmental sampling. Consequently, it is difficult for an independent reviewer to understand the auditors' judgments regarding the audit approach and the sufficiency of the auditors' conclusions.

Effect on the Audit

In general, without sufficient working paper documentation, independent reviewers cannot understand the auditors' conclusions and judgments regarding the work performed. Without sufficient documentation of the auditors' understanding of internal controls, the attributes tested for compliance, and the sampling plan, independent reviewers will not be able to determine that the audit was adequately planned and executed to meet the OMB Circular A-133 audit objectives. Federal agencies rely on the reported opinion on compliance for each major program as appropriate, based on an audit that is conducted in accordance with the requirements of OMB Circular A-133. Without sufficient working paper documentation, there is no evidence that the audit work was performed in accordance with the requirements of OMB Circular A-133, its related Compliance Supplement, GAGAS, and the AICPA auditing standards.

Recommendations, Management's Response, and Evaluation of Response

We recommend that for current and future audits, the Defense Contract Audit Agency document in its working papers the:

- 1. Five components of internal control for each of the compliance requirements within the audit scope.**
- 2. Attributes and criteria tested to support that the audit objectives have been met and to support the opinion on compliance.**

3. Sampling plan used to determine the extent of compliance testing.

Management's Response. Partially concur. Management agrees that the documentation supporting the review could provide a better summary of the auditors' understanding of internal controls; however, the work performed can be relied on to support the audit conclusions. Further, some of the working papers address the organizational controls, but the majority of the working papers focus on the research and development major program.

DCAA improved the internal control documentation for each of the applicable compliance requirements by including additional working papers and references. The auditors reorganized the documentation in the audit files to provide a clearer identification of the five components of internal control and how they relate to the compliance requirements identified in the audit scope. In addition, the auditors revised the permanent files to create a summary of their understanding of the Smithsonian internal control system. The permanent files also summarize the auditor's conclusions regarding the internal controls.

The auditors added a summary in the FY 1999 audit files of the attributes and criteria tested for each of the selected transaction items. The revised working papers identify the specific attributes and criteria tested to allow the reviewer to assess the compliance with the audit program steps and to understand the overall audit conclusions.

The auditors documented the working papers for their intention not to perform a statistical sample. The auditors also provided other data in the working papers that summarizes the universe and the nature of the items selected for compliance testing.

In addition to the completed actions identified above, DCAA plans to conduct staff training on the requirements for adequate working paper documentation, specifically on OMB Circular A-133 audits, and work with Headquarters DCAA to develop and/or improve a working paper package for all future OMB Circular A-133 audits.

Evaluation of Management's Response. We consider management's comments and completed corrective actions responsive to the intent of the recommendations. Therefore, the recommendations are dispositioned and closed.

Finding B. Internal Control Planning and Testing

The DCAA auditors did not plan or test internal controls for the compliance requirements within their audit scope. This occurred because the auditors did not change their historical audit approach to test internal controls for each compliance requirement that has a direct and material effect on each major program as required by OMB Circular A-133. As a result, Federal agencies and other report users cannot rely on the internal control assurances in the audit report.

Internal Control Requirements. In general, OMB Circular A-133 §__500(c) requires the auditor to perform procedures to obtain an understanding of internal controls over Federal programs that is sufficient to plan the audit for major programs¹⁷ and to plan and perform internal control testing. The AICPA SOP 98-3, “Audits of States, Local Governments, and Not-for-Profit Organizations Receiving Federal Awards,” sections 8.7, 8.10, and 8.16, describe the auditors’ responsibilities for planning the review of internal controls for major programs. The auditors must obtain a sufficient understanding of internal control over Federal programs by performing procedures to understand the design of the five internal control components (control environment; risk assessment; control activities; information and communication; and monitoring) related to the A-133 compliance requirements¹⁸ for each major program. The auditors must also determine whether the internal controls are operating. The auditors plan the internal control testing to support a low assessed level of control risk for the assertions¹⁹ relevant to the compliance requirements for each major program. SOP 98-3, section 8.16, explains:

“... [F]ederal agencies want to know if conditions indicate that auditees have not implemented adequate internal control over compliance for federal programs to ensure compliance with applicable laws and regulations.”

The OMB Circular A-133 Compliance Supplement, Part 6, provides guidance on reviewing the five components of internal controls for each type of compliance requirement. The information in the Supplement is intended to assist non-Federal entities

¹⁷See footnote 1.

¹⁸Appendix A identifies the compliance requirements.

¹⁹Assertions are explicit or implicit representations by management that are embodied in financial statement elements (assets, liabilities, revenue, and expenses). The assertions are:

- Existence/Occurrence. The entity’s assets exist, and the transactions that produced them actually occurred.
- Completeness. The financial statements reflect a complete record of all transactions that occurred, and none are omitted.
- Rights/Obligations. The entity has valid title to all assets and real obligations for all liabilities.
- Valuation/Allocation. The correct methods were used to place values on the assets, and the transactions have been assigned to the correct periods.
- Presentation/Disclosure. All the disclosures necessary for full and complete presentation are included in the financial statements.

and their auditors in complying with the internal control requirements by describing the objectives of internal controls and certain characteristics that when present and operating effectively, may ensure compliance with the program requirements.

DCAA Audit Work. As stated in Finding A, the auditors did not document their understanding of internal controls. The DCAA auditors also did not plan or execute the test of the internal controls for the compliance requirements within their audit scope. This occurred because the auditors did not change their historical audit approach to auditing internal controls, which is to review internal controls at the organization level. Historically, the auditors have used their permanent file documentation, which describes internal controls for the entire organization, but not at the compliance requirement level as required by the Circular. OMB Circular A-133 requires a review of internal controls for each compliance requirement that has a direct and material effect on each major program.

DCAA Circular A-133 Standard Working Papers. DCAA Headquarters prepared a draft working paper package that addressed the OMB Circular A-133 auditing and documentation requirements by compliance requirement. The working paper package had not been finalized and, therefore, the auditors did not use it.

Effect on the Audit

Without sufficient documentary evidence to support the review and test of internal controls, an independent reviewer cannot understand the auditors' basis to rely on internal controls and whether reportable conditions or material noncompliance exist within the major program. In addition, Federal agencies cannot rely on the audit report's assurance that internal controls are in place and operating effectively for the major programs that are identified in the audit report. Also, an independent reviewer does not know the auditors' basis for the conclusions on internal control and, therefore, the reviewer has no basis to rely on the Foundation's internal controls. Finally, without the internal control assurance the nature and extent of the auditors' testing for compliance are inadequate to support an opinion.

Recommendations, Management's Response, and Evaluation of Response

4. We recommend that DCAA plan and perform internal control testing for the compliance requirements within their audit scope for the current and future years' audits.

5. We recommend that DCAA use the draft OMB Circular A-133 working paper package to ensure that the audits meet the auditing requirements of the Circular for future years' audits.

Management's Response. Partially concur. DCAA disagrees with the report conclusion, but agrees with the recommendations. The auditors tested the internal controls for the applicable compliance requirements and, therefore, the internal control assurances in the audit report can be relied on. Nevertheless, the auditors have taken steps to improve the internal control planning and testing documentation. Specifically, the auditors improved the internal control testing documentation for the applicable compliance requirements for the FY1999 audit.

The auditors revised the working papers to include the draft OMB Circular A-133 working paper package. In addition, the auditors recommended to Headquarters DCAA that the agency use the draft OMB Circular A-133 working paper package.

Evaluation of Management's Response. We consider management's comments and completed corrective actions responsive to the intent of the recommendations. Therefore, the recommendations are dispositioned and closed.

Finding C. Procurement Audit

The DCAA auditors did not plan, execute, and document an annual review and test of the procurement compliance requirement to meet the OMB Circular A-133 audit requirement. DCAA did not review the work of nonauditors to determine whether the work is reliable. In addition, DCAA used the September 19, 1997, report issued by the nonauditors that is based on work from about 3 years ago and may not represent the current conditions. As a result, there is no basis to rely on the current year's procurement processes at the Smithsonian.

Procurement Testing Requirements

As discussed in Finding A, OMB Circular A-133 and AICPA SOP 98-3 require the auditors to determine compliance with the laws, regulations, and contract and grant provisions that materially affect the major program that includes transaction testing and other auditing procedures to support an opinion on compliance. AICPA SOP 98-3, sections 6.39, 6.36, and 6.37 state that the purpose of the compliance testing is for the auditors to apply procedures to provide reasonable assurance of detecting material noncompliance to determine whether the auditee materially complied with the compliance requirements.

Part 3, section I, of the Compliance Supplement provides the auditors guidance to review compliance for the procurement requirement. The auditors must satisfy the audit objectives to determine compliance and may use the suggested audit procedures contained in the Supplement. Part 3, section I, of the Compliance Supplement states that the auditors must determine whether:

1. Procurements were made in compliance with the provisions of the A-102 Common Rule, OMB Circular A-110, and other procurement requirements specific to an award.
2. The non-Federal entity obtained the required certifications for covered contracts and subawards.

Auditor Qualifications

OMB Circular A-133 §___.105 defines an auditor as "...a public accountant or a Federal, State or local government audit organization, which meets the general standards specified in GAGAS." GAGAS, Chapter 3, describes the following general standards for conducting financial and performance audits: staff qualifications, independence, due professional care, and the presence of quality controls. In general, the audit organization has the responsibility to ensure that the staff conducting each audit collectively has the knowledge and skills necessary for that audit and that its staff maintains professional proficiency through continuing education and training. In addition, the audit organization and the individual auditors should be free from impairments to independence and should maintain an independent attitude and appearance in all matters related to the audit work. The auditors must perform the work with due professional care, which imposes a responsibility on each auditor to observe GAGAS. Finally, each audit

organization conducting audits in accordance with these standards should have an appropriate internal quality control system in place and undergo an external quality control review at least once every 3 years. General standards apply to all audit organizations, both government and non-government that conduct "... audits of government organizations, programs, activities, and functions and of government assistance received by non-government organizations."

Nonauditors

The auditors determined that the procurement compliance requirement has a direct and material effect on the research and development program at the Smithsonian Astrophysical Observatory and that DCAA is responsible for auditing this requirement. The DCAA auditors used the results of a review of the Smithsonian's procurement system by an organization that does not meet the OMB Circular A-133 definition of an auditor. The Department of Defense's Office of Naval Research (ONR) reviewed, approved, and issued a report dated September 9, 1997, on the Smithsonian's procurement system. ONR is not an audit organization and does not perform audits or reviews in accordance with GAGAS. Therefore, DCAA must review the ONR procurement work to determine the extent to which DCAA may rely on the ONR work to meet the OMB Circular A-133 audit requirements. However, the DCAA auditors did not review the ONR organization to determine whether it meets the OMB Circular A-133 auditor definition, and they did not determine whether the auditors' work satisfies the audit objectives for the procurement compliance requirement. Also, the DCAA auditors used the results of a review of the procurement system at the organization level instead of the major program level as required by the Circular. Finally, although the Circular requires an annual audit of the compliance requirements, the auditors used results from 1997 for the 1999 fiscal year audit. This occurred because the DCAA auditors historically had participated on the ONR procurement reviews and believed that because they were familiar with the audit procedures, they understood the objectives of the procurement review and could accept the ONR work.

Effect on the Audit

The DCAA auditors did not audit the procurement compliance requirement for the Smithsonian's fiscal year 1999. The auditors determined that the procurement requirement materially affects the research and development program and, therefore, without an audit of this requirement, the audit is incomplete. In addition, Federal agencies and other report users cannot rely on the report opinion on compliance because DCAA did not audit a major program requirement.

Recommendation, Management's Response, and Evaluation of Response

6. We recommend that DCAA audit the procurement compliance requirement in accordance with OMB Circular A-133 and its related Compliance Supplement for the current and future year's audit, including determining the extent of reliance that can be placed on the work of ONR.

Management's Response. Partially concur. The Circular requires an annual assessment of internal controls. The DCAA assessment of the internal controls was based on the report prepared by the ONR. DCAA appropriately used the ONR report as a tool for assessing risk. Because the contractor has been assessed as low risk based on materiality and prior audit findings and because there were no major changes to the procurement system, it is appropriate to base the assessment of the procurement internal controls on the ONR review provided the auditors have an understanding of the scope performed.

However, the auditors revised the permanent files to reflect the current year's status of the Smithsonian's compliance with suspension and debarment activities, which is a key element in the validation of the procurement system under the OMB Circular A-133 compliance supplement. The working papers now provide sufficient documentation as a basis to rely on the current year's procurement system.

Evaluation of Management's Response. We consider management's comments and completed corrective actions responsive to the intent of the recommendation. Therefore, the recommendation is dispositioned and closed.

Appendix A. Single Audit Requirements

The Inspector General Act of 1978, as amended (Public Law 95-452), requires an agency's Inspector General to "take appropriate steps to assure that any work performed by non-Federal auditors complies with the standards established by the Comptroller General."

The Single Audit Act of 1984 (Public Law 98-502) was intended to improve the financial management of state and local governments, while OMB Circular A-133 was intended to improve financial management for nonprofit organizations. The Act and the Circular established uniform requirements for audits of Federal financial assistance, promoted efficient and effective use of audit resources, and helped to ensure that Federal departments and agencies rely on and use the audit work to the maximum extent practicable.

The Single Audit Act Amendments of 1996 (Public Law 104-156) incorporate the previously excluded nonprofit organizations. Including the nonprofit organizations strengthens the usefulness of the audits by establishing one uniform set of auditing and reporting requirements for all Federal award recipients that are required to obtain a single audit. Major changes to the Act include: (1) increasing the audit threshold from \$25,000 to \$300,000 with respect to Federal financial assistance programs before an audit is required; (2) selecting Federal programs for audit based on a risk assessment rather than the amount of funds involved; and (3) improving the contents and timeliness of single audits.

OMB issued the revised Circular A-133 on June 24, 1997, pursuant to the Single Audit Act Amendments of 1996. In general, the Circular requires that an auditee who expends \$300,000 or more annually in Federal awards, obtain an audit and issue a report of its Federal award expenditures in accordance with the GAGAS applicable to financial audits. The audit must be performed by auditors who meet the independent standards in GAGAS and in accordance with the auditing and reporting requirements of the Circular and its related Compliance Supplement. The audit report submission contains the:

- financial statements and related opinion,
- Schedule of Expenditures of Federal Awards and related opinion,
- report on the internal controls and compliance review of the financial statements,
- report on internal controls reviewed and compliance opinion on major programs,
and
- Schedule of Findings and Questioned Costs.

Appendix A

The auditee must also submit a Data Collection Form to the Department of Commerce Clearinghouse. The form summarizes the significant information in the audit report for dissemination to the public through the Internet. Responsible officials from the audited entity and the audit organization sign the form certifying to the information presented.

The Compliance Supplement is based on the requirements of the Single Audit Act Amendments of 1996 and the final June 24, 1997, revision of OMB Circular A-133, which provide for the issuance of a compliance supplement to assist auditors in performing the required audits. The National State Auditors Association study states:

The Compliance Supplement provides an invaluable tool to both Federal agencies and auditors in setting forth the important provisions of Federal assistance programs. This tool allows Federal agencies to effectively communicate items which they believe are important to the successful management of the program and legislative intent

Compliance with the Supplement satisfies the requirements of OMB Circular A-133. The Supplement identifies Federal programs by Federal agency. The Supplement identifies existing, important, compliance requirements, which the Federal Government expects the auditors to consider as part of an audit required by the 1996 Amendments. Using the Supplement eliminates the need for the auditors to research the laws and regulations for each major program audit to determine the compliance requirements that are important to the Federal Government and that could have a direct and material effect on the major program. The Supplement is a more efficient and cost-effective approach to performing this research. It "... provides a source of information for auditors to understand the Federal program's objectives, procedures, and compliance requirements relevant to the audit as well as audit objectives and suggested audit procedures for determining compliance with the requirements."

For single audits, the Supplement replaces agency audit guides and other audit requirement documents for individual Federal programs and specifically states which of the following 14 compliance requirements are applicable to a major program that may be audited:

1. Activities Allowed or Unallowed
2. Allowable Costs/Cost Principles
3. Cash Management
4. Davis-Bacon Act
5. Eligibility
6. Equipment and Real Property Management
7. Matching, Level of Effort, Earmarking
8. Period of Availability of Federal Funds

9. Procurement and Suspension and Debarment
10. Program Income
11. Real Property Acquisition/Relocation Assistance
12. Reporting
13. Subrecipient Monitoring
14. Special Tests and Provisions

The Compliance Supplement assists the auditors in determining the audit scope for the Circular's internal control requirements. For each compliance requirement, the Supplement describes the objectives of internal control and certain characteristics that when present and operating effectively, may ensure compliance with program requirements. The Supplement gives examples of the common characteristics for the 5 components of internal controls (control environment, risk assessment, control activities, information and communication, and monitoring) for the 14 compliance requirements.

Appendix B. Objectives and Scope

Audit Report Review

The objective of an audit report review is to determine whether the report submitted by the auditee meets the applicable reporting standards and the OMB Circular A-133 reporting requirements. The National Aeronautics and Space Administration (NASA) is the cognizant audit agency for the Smithsonian Institution. KPMG LLP and the Defense Contract Audit Agency (DCAA) jointly audited the report for the Smithsonian Institution's fiscal year ended September 30, 1999. We reviewed the reports for compliance with the requirements of the Single Audit Act, Single Audit Act of 1996, and Amendments, and OMB Circular A-133. We focused our review on the reports' qualitative aspects of (1) due professional care; (2) auditors' qualifications and independence; (3) financial statements, compliance, and internal control reporting; (4) Schedule of Expenditures of Federal Awards; and (5) Schedule of Findings and Questioned Costs.

Quality Control Review

The objectives of a quality control review are to ensure that an audit was conducted in accordance with GAGAS²⁰ and generally accepted auditing standards and whether the audit meets the auditing and reporting requirements of OMB Circular A-133. NASA is the cognizant audit agency for the Smithsonian Institution. We performed a quality control review of the KPMG LLP and DCAA joint audit of the Institution's fiscal year ended September 30, 1999. We focused the review on the audit's qualitative aspects of:

- auditors' qualifications,
- independence,
- due professional care,
- quality control,
- planning and supervision,
- Federal receivables and payables,
- major program determination,
- internal controls and compliance testing for major programs,
- Schedule of Expenditures of Federal Awards,
- Schedule of Findings and Questioned Costs, and
- Data Collection Form.

²⁰These standards are broad statements of the auditors' responsibilities, promulgated by the Comptroller General of the United States.

We organized our review by the general and field work audit standards and the required elements of a single audit. We emphasized the areas of major concern to the Federal Government such as determining and auditing major program compliance and internal controls. We conducted the review July 11-13, 1999, at the Columbia, Maryland, office of DCAA, and July 14-18 at the office of KPMG LLP in Washington, D.C. On July 19 and August 7, 2000, we retested transactions at the Smithsonian that were already tested by DCAA and KPMG.

External Quality Control Review Report

We reviewed the December 16, 1999, report on the most recent peer review of KPMG LLP, performed by PricewaterhouseCoopers LLP. PricewaterhouseCoopers LLP determined that KPMG LLP met the objectives of the quality control review standards established by the American Institute of Certified Public Accountants and that KPMG LLP complied with the standards during the fiscal year ended September 30, 1999.

We reviewed the September 27, 2000, external quality control report of DCAA, performed by the Office of Inspector General, Department of Defense (OIG, DoD). The OIG, DoD determined that there were no material, uncorrected noncompliances with applicable auditing standards or audit policies and procedures for DCAA fiscal years 1997 through 1999.

Appendix C. Quality Control Review Methodology

KPMG LLP Independent Auditors' Report on Financial Statements and Supplementary Schedules of Expenditures of Federal Awards

The auditors are required to determine whether the financial statements are presented fairly in all material respects in conformity with generally accepted auditing principles and are free of material misstatement. We reviewed the audit programs and the testing of evidence to determine whether testing was sufficient based on an assessment of control risk to warrant the conclusion reached. We also reviewed the working papers to determine whether they supported the conclusion.

The auditors are also required to subject the Schedule of Expenditures of Federal Awards to the procedures applicable to the audit of the financial statements and to ensure that the amounts are fairly stated in relation to the basic financial statements. We reviewed the audit programs and the testing of evidence to determine whether testing was sufficient based on an assessment of control risk to warrant the conclusion reached. We also reviewed the working papers to determine whether they supported the conclusion.

KPMG Schedule of Expenditures of Federal Awards

The recipient is responsible for creating the Schedule of Expenditures of Federal Awards and the accompanying notes to the Schedule. The auditors are required to audit the information in the Schedule and to review the notes to ensure it is fairly presented in all material respects in relation to the financial statements taken as a whole. We reviewed the audit programs and the testing of evidence to determine whether testing was sufficient based on an assessment of control risk to warrant the conclusion reached. We also reviewed the working papers to determine whether they supported the conclusion.

KPMG Report on Compliance and on Internal Control over Financial Reporting Based on an Audit of Financial Statements Performed in Accordance with Government Auditing Standards

The auditors are required to determine whether the recipient has complied with laws and regulations that may have a direct and material effect in determining financial statement amounts. The auditors are also required to obtain an understanding of internal controls that is sufficient to plan the audit and to assess control risk. We reviewed the audit programs for the appropriate procedures, the working paper documentation, and the compliance and substantive testing performed.

KPMG Report on Compliance with Requirements Applicable to its Major Programs and on Internal Control Over Compliance in Accordance with OMB Circular A-133; and

DCAA Report on Smithsonian Astrophysical Observatory's Compliance with Requirements Applicable to Major Program(s) and on Internal Control Over Compliance in Accordance with OMB Circular A-133, Fiscal Year 1999; and

DCAA Report on Smithsonian Institution's Compliance with Requirements Applicable to Major Program(s) and on Internal Control Over Compliance in Accordance with OMB Circular A-133, Fiscal Year 1999

The auditors are required to determine whether the recipient has complied with laws, regulations, and the provisions of contracts and grant agreements that may have a direct and material effect on each of its major Federal programs. The auditors are required to use the procedures in the OMB Circular A-133 Compliance Supplement (April 1999) to determine the compliance requirements for each major program. We reviewed the audit program for the appropriate procedures and compared the audit program steps to those in the Compliance Supplement to determine whether the applicable steps had been performed. We reviewed the working paper documentation and its support and the compliance tests performed. We also retested selected expenditures that were already tested by the DCAA and KPMG auditors. See Findings A and B for additional details regarding compliance related to the DCAA work.

The auditors must perform procedures to obtain an understanding of internal controls over Federal programs that is sufficient to plan an audit to support a low-assessed level of control risk for major programs. The auditors must plan and perform internal controls testing over major programs to support a low level of control risk for the assertions relevant to the compliance requirements for each major program. We were unable to review the DCAA audit programs for the appropriate procedures, the working paper documentation, and the test of controls performed. See Finding A for additional details regarding internal controls related to the DCAA work.

KPMG Schedule of Findings and Questioned Costs

The auditors are required to prepare a Schedule of Findings and Questioned Costs that summarizes the audit results. This schedule includes information about and related to the audit that is not required to be identified in other parts of the audit report including: (1) major programs audited, (2) details on findings and questioned costs (including reportable conditions and material weaknesses), (3) dollar threshold to identify major programs, and (4) whether the recipient is considered to be low risk. We reviewed the audit programs for the

appropriate procedures and the working paper documentation supporting the information in the schedule.

Appendix D. Defense Contract Audit Agency Comments



DEFENSE CONTRACT AUDIT AGENCY
DEPARTMENT OF DEFENSE
8725 JOHN J. KINGMAN ROAD, SUITE 2135
FORT BELVOIR, VA 22060-6219

IN REPLY REFER TO

PQA 225.4

October 24, 2000

Mr. Russel A. Rau
Assistant Inspector General for Auditing
Office of Inspector General
National Aeronautics and Space Administration, Headquarters
Washington, DC 20546-0001

SUBJECT: Comments on Draft Quality Control Review Report - Assignment # A09004900

Dear Mr. Rau:

Thank you for the opportunity to respond to the referenced draft report. We also appreciate the extension of time you gave us to submit a written response and your willingness to have Ms. Vera Garratt of your staff evaluate the DCAA actions taken in response to your recommendations.

Attached is our response to the three findings and six recommendations contained in the draft report. We have improved the documentation in the working papers and permanent file to provide a more clear and concise support of the audit work performed. Ms. Garratt has reviewed the revised working papers. I hope now we are both in agreement that the problems identified in the draft have been corrected and that DCAA's audit reports may be relied upon.

We also shared with Ms. Garratt steps we are taking to change Agency policy pertaining to Circular A-133 audits -- specifically, implementation of an A-133 audit program that should help ensure effective audit execution. Additionally, next month the Columbia Branch Office will conduct staff training to re-emphasize the audit requirements of Circular A-133. These actions will help ensure that future DCAA audit effort results in complete and adequate Circular A-133 audits.

Barbara Reilly, Mid-Atlantic regional director, and I would be happy to meet with you if you have any additional questions regarding DCAA's audit coverage at the Smithsonian Institution. Please call [(703) 767-3280] or e-mail me [larry.uhlfelder@dcaa.mil] if you would like to meet or if you have any questions.

Sincerely,

Lawrence P. Uhlfelder
Assistant Director
Policy and Plans

Enclosure
a/s



MID-ATLANTIC REGION
DEFENSE CONTRACT AUDIT AGENCY
ONE INDEPENDENCE MALL
615 CHESTNUT STREET, SUITE 1000
PHILADELPHIA, PA 19106-4498
FAX (215) 597-3533

IN REPLY REFER TO

24 October 2000

MEMORANDUM FOR DIRECTOR, DCAA

ATTENTION: P

Subject: Response to the Office of NASA, Inspector General's (IG) Draft Report on Quality Control Review of Audit of Smithsonian Institution

This memorandum provides the response to the NASA IG draft report dated 11 September 2000, Subject: Quality Control Review of KPMG LLP and Defense Contract Audit Agency Audit of Smithsonian Institution, Fiscal Year Ended September 30, 1999.

Background.

As the cognizant agency for the Smithsonian Institution, the NASA IG reviewed the Office of Management and Budget (OMB) Circular A-133, "Audits of States, Local Governments, and Non-Profit Organizations," performed for the Smithsonian Institution fiscal year ending 30 September 1999. The objectives of their review were to determine whether KPMG and DCAA conducted the audit in accordance with applicable standards and whether the audit meets the auditing and reporting requirements of OMB Circular A-133.

As a result of their review, the NASA IG provided three findings, containing six recommendations for corrective action. We appreciate the NASA IG recommendations and have improved our workpaper documentation by completing the actions on all of the recommendations. We request that headquarters also comment on recommendation No. 5. since it has agency-wide implications. Below is a brief description of the draft findings and our response.

Finding A: Working Paper Documentation

Condition:

"The DCAA auditors did not document their working papers for (1) their understanding of internal controls, (2) the compliance attributes tested, and (3) the audit sampling plan. This occurred because the auditors relied on their past audit experience and on DCAA's historical method of assessing internal control at the organization level rather than at the compliance requirement level. As a result, Federal agencies and other report users cannot rely on the OMB Circular A-133 audit report related to the DCAA audit scope."

Enclosure

Appendix D

SUBJECT: DCAA's Response to NASA IG Draft Report on Quality Control Review –
Smithsonian Institution

NASA IG Recommendations:

We recommend that for the current and future audits, the Defense Contract Audit Agency document in its working papers the:

1. Five components of internal control for each of the compliance requirements within the audit scope.
2. Attributes and criteria tested to support that the audit objectives have been met and to support the opinion on compliance.
3. Sampling plan used to determine the extent of compliance testing.

DCAA Response:

Partially Concur. Although, we concur that the documentation supporting this review is incomplete in some respects and should be better summarized to show a complete understanding of internal controls, we believe that the work performed can be relied upon to support our audit conclusions. Further, while our working papers do address at first the organizational controls, the vast majority of the working papers are focused on the major program of Research and Development.

We have taken the following actions on the NASA IG recommendations 1-3.

1. We have improved the documentation of the five components of internal control for each of the applicable compliance requirements.

For all items identified as incomplete we added additional working papers and references as necessary. We reorganized the documentation in our files to conform to a clearer identification of the five components of internal control and how they relate to the compliance requirements of the audit scope. We created a concise summary of our understanding of the system of internal controls in the Smithsonian permanent file which not only documents the system but provides the auditor's summary of the conclusions regarding the internal controls.

In addition to the items detailed above which deal with actions we have already taken, we also plan to accomplish the items below in an effort to provide a platform of continual improvement in the critical area of OMB A-133 audits.

- Conduct staff training on the requirements for adequate working paper documentation, specifically in OMB Circular A-133 audits.
- Work with Headquarters DCAA to develop/improve a draft OMB Circular A-133 working paper package for all future OMB Circular A-133 audits.

SUBJECT: DCAA's Response to NASA IG Draft Report on Quality Control Review –
Smithsonian Institution

2. We have added a summary of the attributes and criteria tested for each of the selected items in the FY1999 audit files of the Smithsonian to significantly improve the understanding of the attributes tested and the results of the selected items. The revised workpapers detail the specific attributes and criteria tested to allow the reviewer to quickly assess the compliance with the audit program steps and to the overall audit conclusions.
3. We have documented in the workpapers, the auditor's intention not to perform a statistical sample. We have also provided more data in a summary fashion regarding the universe and the nature of the selection of the items utilized for compliance testing.

Finding B: Internal Control Planning and Testing

Condition:

"The DCAA auditors did not plan or test internal controls for the compliance requirements within their audit scope. This occurred because the auditors did not change their historical audit approach to test internal controls for each compliance requirement that has a direct and material effect on each major program as required by OMB Circular A-133. As a result, Federal agencies and other report users cannot rely on the internal control assurances in the audit report."

NASA IG Recommendations:

4. We recommend that DCAA plan and perform internal control testing for the compliance requirements within their audit scope for the current and future years' audits.
5. We recommend that DCAA use the draft OMB Circular A-133 working paper package to ensure that the audits meet the auditing requirements of the Circular for future years' audits.

DCAA Response:

Partially concur. We disagree with the conclusion, but do concur with the recommendations. We tested the internal controls for the applicable compliance requirements and believe that the internal control assurances in the audit report can be relied upon. Nevertheless, we have taken various steps to improve the documentation as it relates specifically to internal control planning and testing and NASA IG recommendations 4 and 5.

4. We have improved the documentation of internal control testing for the applicable compliance requirements for the FY1999 audit.

Appendix D

SUBJECT: DCAA's Response to NASA IG Draft Report on Quality Control Review –
Smithsonian Institution

5. We have revised the working papers to incorporate the draft OMB Circular A-133 working paper package. In addition we have referred the use of the draft OMB Circular A-133 working paper package to Headquarters DCAA for agency-wide consideration.

Finding C: Procurement Audit

Condition:

"The DCAA auditors did not plan, execute, and document an annual review and test of the procurement compliance requirement to meet the OMB Circular A-133 audit requirement. DCAA did not review the work of non-auditors to determine whether the work is reliable. In addition, DCAA used the September 19, 1997, report issued by the non-auditors that is based on work from about 3 years ago and may not represent the current conditions. As a result, there is no basis to rely on the current year's procurement processes at the Smithsonian."

NASA IG Recommendation:

6. We recommend that DCAA audit the procurement compliance requirement in accordance with OMB Circular A-133 and its related Compliance Supplement for the current and future year's audit, including determining the extent of reliance that can be placed on the work of ONR.

DCAA Response:

Partially concur. The Circular requires an assessment of the internal controls on an annual basis. Our assessment of the internal controls was based on the report prepared by the Office of Naval Research (ONR). DCAA appropriately used the ONR report as a tool for assessing risk. Since the contractor has been assessed as low-risk, based on materiality and prior audit findings, and there were no major changes to the system, it is appropriate to base the assessment of the procurement internal controls on the ONR review provided we have an understanding of the scope performed.

However, to address the IGs concern reflected in recommendation No. 6, we updated our permanent files to reflect the current year's status of the Smithsonian's compliance with suspension and debarment activities, which is a key element in the validation of the procurement system under the A-133 compliance supplement. We believe, sufficient documentation now exists as a basis to rely on the current years' procurement system.

SUBJECT: DCAA's Response to NASA IG Draft Report on Quality Control Review –
Smithsonian Institution

Conclusion

As discussed above, we believe that the DCAA audit work performed for the FY1999 Smithsonian OMB Circular A-133 audit can be relied upon. Notwithstanding that conclusion, as noted above, we have implemented the necessary recommended actions to the current Smithsonian FY1999 audit working papers. Our completed actions were presented to Ms. Vera Garrant on 23 October 2000. We appreciate the NASA IG's suggestions and we have improved the documentation in the current audit due to that review.

Please contact me at (215) 597-7451 if you have any questions on this matter.

/s/ Barbara C. Reilly

Barbara C. Reilly
Regional Director

Appendix E. Report Distribution

Audit Firms/Auditors

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Mr. Mark Moser, Branch Manager
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Mr. Earl J. Newman, Jr., Assistant Director of Operations
Headquarters, Defense Contract Audit Agency
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Mr. Larry Uhlfelder, Director
Policy and Plans, Headquarters
Defense Contract Audit Agency
8725 John J. Kingman Highway, Suite 2353
Fort Belvoir, VA 22060-6219

Audited Organization

Mr. Rick Johnson, Chief Financial Officer
Smithsonian Institution
955 L'Enfant Plaza, SW, Room 7400
Washington, DC 20560

Federal Offices of Inspector General

Agency for International Development
Department of Agriculture
Department of Commerce
Department of Defense
Department of Education
Department of Energy
Department of Health and Human Services
Department of the Interior
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National Science Foundation
United States Post Office

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AI/Associate Deputy Administrator
AO/Chief Information Officer
B/Chief Financial Officer
B/Comptroller
BF/Director, Financial Management Division
G/General Counsel
H/Associate Administrator for Procurement
JM/Acting Director, Management Assessment Division

NASA Centers

Director, Ames Research Center
Director, Goddard Space Flight Center
Director, Langley Research Center
Director, Marshall Space Center

Major Contributors to the Report

Patrick A. Iler, Program Director, Audit Quality

Vera J. Garrant, Auditor-in-Charge

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Machelle Souverain, Intern

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Tewana Hoskins, Program Assistant

NASA Assistant Inspector General for Auditing Reader Survey

The NASA Office of Inspector General has a continuing interest in improving the usefulness of our reports. We wish to make our reports responsive to our customers' interests, consistent with our statutory responsibility. Could you help us by completing our reader survey? For your convenience, the questionnaire can be completed electronically through our homepage at <http://www.hq.nasa.gov/office/oig/hq/audits.html> or can be mailed to the Assistant Inspector General for Auditing; NASA Headquarters, Code W, Washington, DC 20546-0001.

Report Title: Quality Control Review of KPMG LLP and Defense Contract Audit Agency Audit of Smithsonian Institution for Fiscal Year Ended September 30, 1999 (Assignment No. A0004900)

Report Number: _____ **Report Date:** _____

Circle the appropriate rating for the following statements.

	Strongly Agree	Agree	Neutra l	Disagre e	Strongl y Disagre e	N/A
1. The report was clear, readable, and logically organized.	5	4	3	2	1	N/A
2. The report was concise and to the point.	5	4	3	2	1	N/A
3. We effectively communicated the audit objectives, scope, and methodology.	5	4	3	2	1	N/A
4. The report contained sufficient information to support the finding(s) in a balanced and objective manner.	5	4	3	2	1	N/A

Overall, how would you rate the report?

Excellent Fair Very Good Poor Good

If you have any additional comments or wish to elaborate on any of the above responses, please write them here. Use additional paper if necessary.

How did you use the report?

How could we improve our report?

How would you identify yourself? (Select one)

Congressional Staff	Media
NASA Employee	Public Interest
Private Citizen	Other: _____
Government: _____	Federal: _____ State: _____ Local: _____

May we contact you about your comments?

____ Yes.
Name _____

Telephone Number: _____

____ No.

Thank you for your cooperation in completing this survey.

MAILING LABELS

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