

National Aeronautics and Space Administration
Office of Inspector General
Washington, DC 20546-0001



November 16, 2009

TO: Administrator
Chief Financial Officer

FROM: Acting Inspector General

SUBJECT: Audit of the National Aeronautics and Space Administration's
Fiscal Year 2009 Special-Purpose Financial Statements (Report
No. IG-10-004; Assignment No. A-09-006-02)

Under the Chief Financial Officers Act of 1990, NASA's financial statements are to be audited in accordance with generally accepted government auditing standards. The Office of Inspector General contracted with the independent public accounting firm Ernst & Young LLP (E&Y) to audit NASA's special-purpose financial statements in accordance with the Government Accountability Office's "Government Auditing Standards" and the Office of Management and Budget's Bulletin No. 07-04, "Audit Requirements for Federal Financial Statements," as amended. E&Y also reported on NASA's consolidated general-purpose financial statements: "Audit of the National Aeronautics and Space Administration's Fiscal Year 2009 Financial Statements" (Report No. IG-10-002, November 13, 2009).

NASA's special-purpose financial statements were prepared in accordance with the guidance provided in the U.S. Department of the Treasury's Financial Manual (TFM), Volume I, Part 2, Chapter 4700. To assist the Department of the Treasury in preparing the Financial Report of the United States Government, NASA's general-purpose financial statements were reclassified into a standard format for consolidation with those of other Federal agencies. Also, NASA's intragovernmental balances were separated and reported by Federal agency to facilitate the elimination of agency-to-agency transactions.

In the "Report of Independent Auditors" (Enclosure), E&Y disclaimed an opinion on NASA's special-purpose financial statements for the fiscal years ended September 30, 2009 and 2008. While the Agency made significant progress in improving its financial processes and systems, the disclaimer resulted from continued weaknesses in internal controls over accounting for legacy property, plant, and equipment.

In fulfilling our responsibilities, we monitored the progress of the audit, reviewed E&Y's report and related documentation, inquired of its representatives, and ensured that E&Y met contractual requirements. Our review was not intended to enable us to express, and we do not express, an opinion on NASA's special-purpose financial statements, conclusions about the effectiveness of internal controls over financial reporting, or compliance with the TFM.

E&Y is responsible for the enclosed report and the conclusions expressed therein. Our review, while still ongoing, disclosed no instances where E&Y did not comply, in all material respects, with the Government Accountability Office's "Government Auditing Standards."

signed

Thomas J. Howard

Enclosure



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Report of Independent Auditors

To the Administrator and the Acting Inspector General
of the National Aeronautics and Space Administration

We were engaged to audit the accompanying reclassified balance sheets as of September 30, 2009 and 2008, and the related reclassified statements of net cost and changes in net position for the years then ended, (hereinafter referred to as the special-purpose financial statements) contained in the special-purpose closing package of the National Aeronautics and Space Administration (NASA). These special-purpose financial statements are the responsibility of NASA's management.

The accompanying special-purpose financial statements and accompanying notes contained in the special-purpose closing package have been prepared for the purpose of complying with the requirements of the U.S. Department of the Treasury's Financial Manual (TFM) Volume I, Part 2, Chapter 4700 solely for the purpose of providing financial information to the U.S. Department of the Treasury and U.S. Government Accountability Office (GAO) to use in preparing and auditing the *Financial Report of the U.S. Government*, and are not intended to be a complete presentation of NASA's financial statements.

As reported in our Report of Independent Auditors included in NASA's FY 2009 Performance and Accountability Report, during fiscal year (FY) 2009, NASA continued its focused efforts to resolve long term issues identified in its financial management processes and systems. Although significant progress has been made, NASA management and our work continue to identify issues related to internal control in its property accounting principally relating to assets capitalized in prior years. As a result of these limitations, we were unable to obtain sufficient evidential support for the amounts presented in the consolidated balance sheets as of September 30, 2009 and 2008, and the related consolidated statements of net costs, and changes in net position and combined statements of budgetary resources for the fiscal years then ended.

Because of the matters discussed in the preceding paragraph, the scope of our work was not sufficient to enable us to express, and we do not express, an opinion on the reclassified balance sheets as of September 30, 2009 and 2008, and the related reclassified statements of net cost and changes in net position for the fiscal years then ended contained in the special purpose closing package of NASA.

The information included in the Other Data is presented for the purpose of additional analysis and is not a required part of the special-purpose financial statements, but is supplementary information required by the TFM Chapter 4700. We were unable to apply to the information certain procedures prescribed by professional standards, because of the limitations on the scope of our audit of the financial statements, as discussed above.

In accordance with *Government Auditing Standards* and Office of Management and Budget (OMB) Bulletin No. 07-04, *Audit Requirements for Federal Financial Statements*, we have also issued reports dated November 9, 2009, on our consideration of NASA's internal control over financial reporting and its compliance with certain provisions of laws and regulations and other matters. Those reports are an integral part of an audit of principal financial statements performed in accordance with *Government Auditing Standards* and OMB Bulletin No. 07-04, as amended, and should be considered in assessing the results of our work.

In planning and performing our work on the special-purpose financial statements, we also considered NASA's internal control over the financial reporting process for the special-purpose financial statements and compliance with the TFM Chapter 4700. NASA's management is responsible for establishing and maintaining internal control over financial reporting, including Other Data, and for complying with laws and regulations, including compliance with the TFM Chapter 4700 requirements.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control that might be significant deficiencies or material weaknesses and therefore, there can be no assurance that all deficiencies, significant deficiencies, or material weaknesses have been identified. However, as discussed below, we identified certain deficiencies in internal control that we consider to be a material weakness.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. We consider the deficiencies related to Enhancements Needed for Controls over Legacy PP&E and Materials Contracts to be a material weakness.

A significant deficiency is a deficiency or a combination of deficiencies in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. We consider the deficiencies related to Processes in Estimating NASA's Environmental Liability Continue to Require Enhancements and Financial Management Systems Not in Substantial Compliance with FFMA to be significant deficiencies.

Additionally, during our audit procedures related to the special-purpose financial statements, we found instances in which information contained in the special-purpose financial statements needed to be changed (and were) in connection with our work to conform to the information required in the TFM requirements or to agree with information reflected in NASA's FY 2009 Performance and Accountability Report. Our overarching recommendations included in the aforementioned Report on Internal Control are applicable in addressing partially ineffective review processes for the special-purpose financial statements. Our tests of compliance with TFM Chapter 4700 requirements disclosed no additional instances of noncompliance that are required to be reported under *Government Auditing Standards* or OMB Bulletin No. 07-04, as amended. However, providing opinions on internal control over the financial reporting process for the special-purpose financial statements or on compliance with the TFM Chapter 4700 requirements were not objectives of our audit of the special-purpose financial statements and, accordingly, we do not express such opinions. As noted above, we were unable to complete our work in auditing the special-purpose financial statements. Had we done so, other matters might have been reported.

This report is intended solely for the information and use of NASA, the U.S. Department of the Treasury, the OMB and the GAO in connection with the preparation and audit of the Financial Report of the U.S. Government and is not intended to be and should not be used by anyone other than these specified parties.

A handwritten signature in black ink that reads 'Ernst & Young LLP'.

November 16, 2009