

Report Recipients:

Partner, Moore, Stephens,
Apple
Vice President, Operations,
Ohio Aerospace Institute

**MOORE, STEPHENS, APPLE AUDIT OF THE
OHIO AEROSPACE INSTITUTE FOR THE
FISCAL YEAR ENDED JUNE 30, 2002**

December 22, 2003

cc:

JM/Director,
Management
Assessment Division



National Aeronautics and
Space Administration

OFFICE OF INSPECTOR GENERAL

Released by: [Original Signed By]

David M. Cushing, Assistant Inspector General for Auditing

**Moore, Stephens, Apple Audit of the Ohio Aerospace Institute
for the Fiscal Year Ended June 30, 2002**

The Inspector General Act of 1978 (Public Law 95-452), as amended, mandates Inspectors General to ensure that work performed by non-Federal auditors complies with generally accepted government auditing standards (GAGAS) issued by the Comptroller General of the United States. As part of our continuing oversight of non-Federal audit work performed by independent public accountants under the Single Audit Act and the Single Audit Act Amendments of 1996, we performed a quality control review of the Moore, Stephens, Apple audit of the Ohio Aerospace Institute (the Institute) for the fiscal year ended June 30, 2002. The objective of our quality control review was to determine whether the audit working papers and report met the standards and requirements of GAGAS and Office of Management and Budget (OMB) Circular A-133, "Audits of States, Local Governments, and Non-Profit Organizations," and its related Compliance Supplement (the Supplement). The results of our quality control review follow:

- **Working Paper Quality Review.** For the most part, the Moore, Stephens, Apple audit work met GAGAS and the requirements in OMB Circular A-133 and its related Supplement. However, the auditors did not audit the Institute's entire research and development (R&D) major program and did not document some of their conclusions in the working papers. Subsequent to our review, the auditors performed additional testing to audit the entire R&D cluster and documented their conclusions.
- **Audit Report Quality Review.** The audit report met the OMB Circular A-133 reporting requirements except that the data collection form and schedules were incorrect and incomplete. Subsequent to our review, on November 5, 2003, the auditors submitted the correctly completed data collection form and schedules to the Federal Audit Clearinghouse.

Entire Research and Development Major Program Was Not Audited

Moore, Stephens, Apple did not audit the Institute's entire R&D program cluster as the Institute's major program. OMB Circular A-133, §__.105, and Part 5 of the Supplement define a cluster of programs as a grouping of closely related programs that share common compliance requirements and specifically identify R&D as a single cluster of programs. A cluster is then considered by the auditors as one program for determining major programs to be audited. For the fiscal year ended June 30, 2002, all Federal expenditures at the Institute were in the R&D program cluster. Therefore, the R&D program cluster should have been the Institute's only major program and should have been audited in its entirety. However, Moore, Stephens, Apple did not audit the entire R&D program cluster as the major program but audited only a portion of the R&D cluster. The auditors

improperly defined the program clusters as (1) expenditures by the National Aeronautics and Space Administration (NASA) Centers, (2) expenditures by the Department of Defense, (3) expenditures by the Department of Commerce, (4) expenditures by the General Services Administration, and (5) miscellaneous NASA awards. The auditors then incorrectly audited only the expenditures from the NASA Glenn Research Center at Lewis Field as the major program for the fiscal year ended June 30, 2002. Those expenditures represented 68.8 percent of total Federal expenditures.

We had planned to recommend that Moore, Stephens, Apple perform additional testing to audit the entire R&D cluster as the major program. However, based on our discussions with the audit supervisor, the auditors performed additional testing to audit the entire R&D cluster. We considered the corrective action sufficient, and therefore we make no recommendation. As a result of the additional testing, Federal agencies and other report users can now rely on the opinion on compliance and the audit report's assurance that internal controls are in place and operating effectively for the entire R&D program.

Working Papers Were Not Documented in Accordance with GAGAS

Moore, Stephens, Apple did not document its working papers to support its conclusion that 2 of 14 compliance requirements were not applicable to the Institute's R&D program. GAGAS §4.35 requires that working papers contain sufficient information to enable an experienced auditor having no previous connection with the audit to ascertain from them the evidence that supports the auditor's significant conclusions and judgments. Because the working papers did not contain adequate evidence that the compliance requirements were not applicable, we could not determine from the working papers whether the auditors properly performed audit procedures and tested material compliance requirements in making their conclusions about compliance and internal controls for the R&D program.

OMB issued the Compliance Supplement to assist auditors in meeting the requirements of Circular A-133. The Supplement, Part 2, identifies the 14 types of compliance requirements that may apply to an R&D cluster of programs. A compliance requirement may not apply because the auditee has no activity subject to that requirement or the activity does not have a material effect on the major program. Therefore, auditors must determine every year whether each of the 14 compliance requirements applies to the R&D program as well as test all material compliance requirements. The American Institute of Certified Public Accountants (AICPA) Statement of Position (SOP) 98-3 states that the auditor should document the rationale for omitting tests of controls relevant to the nonmaterial requirements. Moore, Stephens, Apple concluded that 2 of the 14 compliance requirements—the Davis Bacon Act and the real property acquisition and relocation assistance—were not applicable to the Institute's R&D program. However, the audit working papers did not explain why the requirements were not applicable.

We had planned to recommend that Moore, Stephens, Apple use guidance in the Supplement and SOP 98-3 to document the reasons the Davis-Bacon Act as well as the

real property acquisition and relocation assistance were not applicable or material to the major program for the fiscal year 2002 audit. After our review, however, the auditors provided revised working papers to correct the deficiencies. We considered the corrective action sufficient, and therefore we make no recommendation to address the documentation deficiencies. Federal agencies and other report users can now rely on the opinion on compliance and the audit report's assurance that internal controls are in place and operating effectively.

Data Collection Form and Schedules Were Prepared Incorrectly

Moore, Stephens, Apple did not correctly prepare the data collection form and schedule of findings and questioned costs (schedule) as required. OMB Circular A-133, §___.320, requires the auditee to submit to the Federal Audit Clearinghouse a data collection form that provides the results of the audit and a reporting package that includes the schedule of expenditures of Federal awards (SEFA). OMB Circular A-133 further requires that the data collection form include the name of each Federal program as well as identification of each major program and that individual programs within a cluster of programs be listed in the same level of detail as they are listed in the SEFA. Moore, Stephens, Apple should have reported the R&D program cluster as the major program on the data collection form and schedule. However, the schedule showed the NASA Glenn Research Center at Lewis Field as the major program, but the data collection form showed all programs as major except the NASA Glenn Research Center at Lewis Field and the NASA miscellaneous programs. Additionally, the individual programs within the R&D program cluster were not listed in the same level of detail on the data collection form as they were reported on the SEFA.

We had planned to recommend that Moore, Stephens, Apple (1) correct the data collection form, schedule of findings and questioned costs, and SEFA to accurately show the R&D cluster of programs as the major program and (2) correct the data collection form to list individual programs within the R&D cluster in the same level of detail as on the SEFA. However, in response to our review, the auditors submitted a correctly completed data collection form to the Federal Audit Clearinghouse on November 5, 2003. We considered the corrective action sufficient, and therefore we make no recommendation to address the documentation deficiencies. Federal agencies can now effectively use the audit results to monitor Federal programs.

Appendixes

Among the appendixes, note that Appendix A contains details on the Circular and Single Audit Act requirements, Appendix B provides details on the objectives and scope of our review, Appendix C provides our quality control review methodology, and Appendix D summarizes the results of the Moore, Stephens, Apple audit of the Institute.

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Acronyms Used in This Report

AICPA	American Institute of Certified Public Accountants
GAGAS	Generally Accepted Government Auditing Standards
OIG	Office of Inspector General
OMB	Office of Management and Budget
R&D	Research and Development
SEFA	Schedule of Expenditures of Federal Awards
SOP	Statement of Position

Appendix A. Single Audit Act Requirements

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, “Audits of States, Local Governments, and Non-Profit Organizations,” was intended to improve financial management for nonprofit organizations. The Act and the Circular establish uniform requirements for audits of Federal financial assistance, promote efficient and effective use of audit resources, and help 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 generally accepted government auditing standards applicable to financial audits. The audit must be performed by auditors who meet the independence standards in GAGAS and in accordance with the auditing and reporting requirements of the Circular and its related Compliance Supplement (the Supplement). The audit report submission contains the:

- financial statements and related opinion,
- SEFA 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.

The auditee must also submit a data collection form to the Federal Audit 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.

Appendix A

The Supplement is based on the requirements of the Single Audit Act Amendments of 1996 and the 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 Circular and 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. The Supplement “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 and Relocation Assistance
12. Reporting
13. Subrecipient Monitoring
14. Special Tests and Provisions

The Supplement also 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. Background, Objectives, and Scope

Background

The Ohio Aerospace Institute (the Institute), incorporated in May 1989 in Cleveland, Ohio, facilitates collaboration among government, industry, and educational institutions primarily in Ohio in aerospace-related technology. For the fiscal year ended June 30, 2002, the Institute reported total Federal expenditures of about \$15.7 million and total NASA expenditures of about \$12.2 million.

Audit Report Review

Our objectives for the audit report review were to determine whether the report submitted by the auditee met reporting standards in GAGAS and met reporting requirements in OMB Circular A-133, “Audits of States, Local Governments, and Non-Profit Organizations.” As the oversight agency for audit for the Institute, the NASA Office of Inspector General (OIG) performed a review of the audit report on the Institute for its fiscal year ended June 30, 2002. We reviewed the report for compliance with the requirements of the Single Audit Act, Single Audit Act Amendments of 1996, and OMB Circular A-133. We focused our review on the report’s qualitative aspects of the (1) financial statement, compliance, and internal control reporting; (2) SEFA; and (3) schedule of findings and questioned costs.

Working Paper Review

Our objectives for the working paper review were to determine whether the audit was conducted in accordance with GAGAS and whether the audit met the requirements of OMB Circular A-133 and its related Compliance Supplement. As the oversight agency for audit for the Institute, the NASA OIG conducted a quality control review of the Moore, Stephens, Apple audit working papers for the R&D program. 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, and
- internal controls and compliance testing for major programs.

We also focused the review on the working paper support for the

- schedule of expenditures of Federal awards,
- schedule of findings and questioned costs, and
- data collection form.

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 April 21 through April 25, 2003, at the Westlake, Ohio, office of Moore, Stephens, Apple. The NASA OIG had not previously performed quality control reviews at other Moore, Stephens, Apple locations.

Peer Review Report

To determine whether there were any issues of which we needed to be aware during our report and working paper review, we assessed the October 4, 2001, report on the most recent peer review of Moore, Stephens, Apple performed by Postlethwaite & Netterville. The Postlethwaite & Netterville review determined that Moore, Stephens, Apple met the objectives of the quality control review standards established by the AICPA and that Moore, Stephens, Apple complied with the standards during the fiscal year ended May 31, 2001.

Appendix C. Quality Control Review Methodology

Report of Independent Auditors

The auditors are required to determine whether the financial statements are presented fairly in all material respects in conformity with generally accepted accounting principles and are free of material misstatement. The auditors are also required to subject the SEFA (schedule) 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 evidence to determine whether testing was sufficient based on an assessment of control risk to warrant the conclusion reached.

Schedule of Expenditures of Federal Awards

The recipient is responsible for creating the schedule and the accompanying notes to the schedule. The auditors are required to audit the information in the schedule and review the notes to ensure that the schedule is presented fairly in all material respects in relation to the financial statements taken as a whole. We reviewed the auditors' procedures for testing the Federal expenditures and reconciling the amounts to the general ledger and trial balance.

Report of Independent Auditors on Compliance and on Internal Control Over Financial Reporting Based on an Audit of the 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 Moore, Stephens, Apple audit program for the appropriate procedures, working paper documentation, and compliance and substantive testing performed.

Report of Independent Auditors on Compliance with Requirements Applicable to Each Major Program and Internal Control Over Compliance in Accordance With OMB Circular A-133

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 to determine the compliance requirements for each major program. Further, the auditor should design the audit to provide reasonable assurance of detecting material misstatements resulting from noncompliance with provisions of contracts or grant agreements that have a direct and

material effect on the determination of financial statement amounts. 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 for the major program. We also reviewed the working paper documentation and the compliance tests performed.

The auditors must also perform procedures to obtain an understanding of internal controls over Federal programs that is sufficient to plan an audit that supports a low-assessed level of control risk for major programs. The auditors must plan and perform internal control 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 reviewed the audit program for the appropriate procedures, the working paper documentation, and the test of controls performed for the major program.

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

Appendix D. Results of the Moore, Stephens, Apple Audit of the Ohio Aerospace Institute for the Fiscal Year Ended June 30, 2002

On September 13, 2002, Moore, Stephens, Apple issued the audit report for the Ohio Aerospace Institute for the fiscal year ended June 30, 2002. The auditors issued an unqualified opinion* on the financial statements; SEFA; and auditee's compliance with laws, regulations, and provisions of contracts or grant agreements that could have a direct and material effect on the major program. However, the auditors incorrectly identified the major program as the NASA expenditures at the Glenn Research Center at Lewis Field. The auditors should have identified the entire R&D cluster as the major program. On November 5, 2003, the auditors submitted a revised reporting package to the Federal Audit Clearinghouse that correctly identified the R&D cluster as the major program.

The auditors identified no findings and questioned costs related to the major program. The auditors also found no instances of noncompliance in the financial statement audit that must be reported under generally accepted government auditing standards. Further, the auditors identified no material weaknesses related to internal controls for the financial statements or major programs. The AICPA SOP 98-3, Appendix D, defines a material weakness as:

. . . a 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.

* An 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 and grant provisions that could have a direct and material effect on each major program.

Appendix E. Report Distribution

Audit Firm

Mr. Roger B. Watkins, Principal
Moore, Stephens, Apple
1540 Market Street
Akron, OH 44313

Audited Organization

Mr. Jake Breland
Vice President, Operations
Ohio Aerospace Institute
22800 Cedar Point Road
Cleveland, OH 44142

Other

Technical Manager
Office of Federal Financial Management
Office of Management and Budget, Office of Federal Financial Management,
New Executive Office of the President
725 17th Street, Room 6025
Washington, DC 20503

Federal Audit Clearinghouse
1201 East 10th Street
Jeffersonville, IN 47132

Federal Offices of Inspector General

Office of Deputy Inspector General for Inspections and Policy
Office of Audit Policy and Oversight
Office of Inspector General
U.S. Department of Defense
400 Army-Navy Drive, Room 737
Arlington, VA 22202-2884

Office of Inspector General
ATTN: Single Audit Contact
U.S. Department of Energy
IG-33, Room 5A-193
1000 Independence Avenue SW
Washington, DC 20585

Appendix E

Federal Offices of Inspector General (continued)

Regional Inspector General for Auditing
General Services Administration
Washington Field Office (JA-W)
7th and D Streets SW, Room 1070
Washington DC, 20407

National Aeronautics and Space Administration (NASA) Officials-in-Charge

AD/Deputy Administrator
AA/Chief of Staff
ADI/Associate Deputy Administrator for Institutions and Asset Management
B/Chief Financial Officer
B/Deputy Chief Financial Officer for Financial Management
B/Deputy Chief Financial Officer for Resources (Comptroller)
BF/Director, Financial Management Division
G/General Counsel
H/Assistant Administrator for Procurement
J/Assistant Administrator for Management Systems
JM/Director, Management Assessment Division

NASA Centers

GRC/100/Director, Glenn Research Center at Lewis Field
GSFC/100/Director, Goddard Space Flight Center
JSC/AA/Director, Lyndon B. Johnson Space Center

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Report Title: "Quality Control Review of the Moore, Stephens, Apple Audit of the Ohio Aerospace Institute for the Fiscal Year Ended June 30, 2002 (Assignment Number A-03-016-00)," Report No. IG-04-006, dated December 22, 2003

Circle the appropriate rating for the following statements.

	Strongly Agree	Agree	Neutral	Disagree	Strongly Disagree	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
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 Good

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