

**QUALITY
CONTROL
REVIEW
REPORT**

**EGGLESTON SMITH P.C. AUDIT OF NATIONAL
AERONAUTICS AND SPACE ADMINISTRATION
LANGLEY RESEARCH CENTER EXCHANGE
FINANCIAL STATEMENTS FOR FISCAL YEAR ENDED
SEPTEMBER 30, 1998**

March 8, 2000



National Aeronautics and
Space Administration

OFFICE OF INSPECTOR GENERAL

Additional Copies

To obtain additional copies of this report, contact the Assistant Inspector General for Auditing at (202) 358-1232, or visit www.hq.nasa.gov/office/oig/hq/issuedaudits.html.

Suggestions for Future Audits

To suggest ideas for or to request future audits, contact the Assistant Inspector General for Auditing. Ideas and requests can also be mailed to:

Assistant Inspector General for Auditing
Code W
NASA Headquarters
Washington, DC 20546-0001

NASA Hotline

To report fraud, waste, abuse, or mismanagement, contact the NASA OIG Hotline at (800) 424-9183, (800) 535-8134 (TDD), or at www.hq.nasa.gov/office/oig/hq/hotline.html#form; or write to the NASA Inspector General, P.O. Box 23089, L'Enfant Plaza Station, Washington, DC 20026. The identity of each writer and caller can be kept confidential, upon request, to the extent permitted by law.

Reader Survey

Please complete the reader survey at the end of this report or at <http://www.hq.nasa.gov/office/oig/hq/audits.html>.

Acronyms

AICPA	American Institute of Certified Public Accountants
FY	Fiscal Year
GAS	Government Auditing Standards
GAAS	Generally Accepted Auditing Standards
NPD	NASA Policy Directive

Office of Inspector General

March 8, 2000

Mr. Russell Meyers
Eggleston Smith P.C.
Certified Public Accountants and Consultants
603 Pilot House Drive, Suite 400
Newport News, VA 23606

Re: Report on Quality Control Review of Eggleston Smith P.C. Audit of the
National Aeronautics and Space Administration Langley Research Center Exchange
Financial Statements for Fiscal Year Ended September 30, 1998
Assignment Number A0001900
Report Number IG-00-013

Dear Mr. Meyers:

The subject final report is provided for your use. Please refer to the Results in Brief for the overall review results.

If you have questions concerning the report, please contact Mr. Patrick A. Iler, Director, Audit Quality, at (216) 433-5408, or Ms. Bonnie Armstrong, Auditor-in-Charge, at (321) 867-4073. We appreciate the courtesies extended to the audit staff. The final report distribution is in Appendix B.

Sincerely,

[original signed by]

Russell A. Rau
Assistant Inspector General for Auditing

Enclosure

cc:

B/Chief Financial Officer

B/Comptroller

BF/Director, Financial Management Division

G/General Counsel

JM/Management Assessment Division

NASA Office of Inspector General

IG-00-013
A0001900

March 8, 2000

Eggleston Smith P.C. Audit of National Aeronautics and Space Administration Langley Research Center Exchange Financial Statements for Fiscal Year Ended September 30, 1998

Introduction

The NASA Office of Inspector General performed a quality control review of the Eggleston Smith P.C. audit of the Langley Research Center Exchange (Langley Exchange) fiscal year (FY) 1998 Financial Statements. For the FY 1998 financial statement audit, the Langley Research Center retained Eggleston Smith P.C., a public accounting firm licensed to operate in the state of Virginia. The Langley Exchange is a Government instrumentality operating under NASA's control. It operates and generates revenues from the employee cafeterias, gift shops, a recreation center, and vending concessions. For the year ended September 30, 1998, the Langley Exchange reported a cash balance of \$222,336¹ and a net loss of \$16,795.

The Inspector General Act of 1978, as amended, mandates Inspectors General to ensure that work performed by non-Federal auditors complies with government auditing standards² (GAS) issued by the Comptroller General of the United States. The GAS incorporate, by reference, the American Institute of Certified Public Accountants (AICPA) standards of field work and reporting.³ Compliance with GAS provides reasonable assurance that:

- Financial statements present fairly the financial condition and results of operations of the Exchange in accordance with established accounting principles.
- Internal controls are in place and operating as intended.
- The Exchange is complying with applicable laws and regulations.

¹ The cash balance also includes certificates of deposit, money market funds, and highly liquid debt instruments with an original maturity of 3 months or less.

² Government auditing standards are broad statements of the auditors' responsibilities, promulgated by the Comptroller General of the United States. The standards apply to audits of government organizations, programs, activities, and functions.

³ GAS prescribe the minimum hours of continuing education requirements and additional standards for field work and reporting.

In contrast to GAS, generally accepted auditing standards (GAAS)⁴ require an audit opinion⁵ only on the financial statements. GAAS do not require reporting on internal controls or compliance with laws and regulations as part of the financial statement audit.

The review objective was to determine whether the independent external auditors performed the audit in accordance with applicable auditing standards and whether the Langley Exchange has taken corrective actions on recommendations resulting from the audit. Appendix A contains additional details on our objectives, scope, and methodology.

Results in Brief

The audit firm, Eggleston Smith P.C., conducted the audit in accordance with GAAS, which are promulgated by the AICPA. As a result, the auditors opined on the fair presentation of the financial statements only. In addition, the audit firm issued a management letter to the Langley Exchange Council that contains recommendations for improvement. According to Eggleston Smith P.C. and the Langley Office of the Chief Financial Officer, the Langley Exchange Council has resolved all the recommendations and implemented corrective actions where required.

The audit opinion was qualified⁶ because the Langley Exchange receives contributions of space and utilities from NASA Langley Research Center for its activities but omitted from the Exchange's financial statements the revenue and expense related to the contributions. In Eggleston Smith's opinion, these omissions are not in accordance with generally accepted accounting principles. The principles require that non-profit organizations include the revenue and expense related to donated space in their financial statements. Subsequent to the issuance of the audit report, the Langley Exchange Council documented that the Langley Exchange was a Government instrumentality operating in compliance with NASA policies based on the Space Act of 1958 and did not need to include donated space and utilities in its financial statements. Eggleston Smith concurred with the Langley Exchange assertions⁷ and considers the issue resolved.

We consider the actions taken by the Langley Exchange to be responsive to Eggleston Smith's recommendations.

⁴ Generally accepted auditing standards, promulgated by the AICPA, are broad statements of the auditors' responsibilities. The standards apply to audits of non-governmental organizations.

⁵ An audit opinion reflects the auditor's conclusions based on the results of the audit examination.

⁶ A qualified audit opinion means that except for the specific condition identified in the qualification, the overall financial statements present fairly, in all material respects, the Exchange's financial position and results of its operations and cash flows.

⁷ Assertions are implied and expressed representations by management about the components of financial statements.

Background

NASA Policy Directive (NPD) 9050.6E, "NASA Exchange Activities," dated December 2, 1997, authorizes Center Directors to establish an Exchange to contribute to the efficiency, welfare, and morale of NASA personnel. Center Directors are required to appoint an Exchange Council to oversee the Exchange operations. The Council must consist of at least five Center employees who perform their duties without pay from the Exchange. Exchange-operated activities are generally self-sustained (that is, supported by nonappropriated funds⁸). The Directive also requires annual audits of the Exchange's financial statements and the submission of the statements and the audit reports to the Center Chief Financial Officer by December 31 annually.

Auditors engaged to conduct the financial audits of the Exchanges have generally followed the GAAS. However, the Inspector General, together with officials from the Offices of the Chief Financial Officer and Management Systems, determined that the audits should be conducted in accordance with GAS because the Exchanges are Government instrumentalities. The Inspector General issued a policy memorandum on March 1, 1999, to all the Exchanges regarding the shift to GAS, which auditors must follow beginning with the FY 1999 financial statement audits.⁹

Independent Auditors' Report

In its November 12, 1998, report, Eggleston Smith P.C. rendered a qualified opinion on the FY 1998 Statements of Financial Position, Activities, and Cash Flows for the Langley Exchange. The opinion was qualified because the Langley Exchange receives contributions of space and utilities from NASA Langley Research Center for its activities but does not include in the Exchange's financial statements the revenue and expense related to these contributions. In Eggleston Smith's opinion, these omissions are not in accordance with generally accepted accounting principles. The principles require that non-profit organizations include the revenue and expense related to donated space in their financial statements.

In a separate management letter to the Langley Exchange Council, Eggleston Smith P.C. recommended the following improvements:

- Develop a system to facilitate reconciliation of sales and purchases of attractions tickets to the general ledger
- Eliminate the practice of backdating checks.

The audit firm's work met applicable requirements contained in GAAS.

⁸ Nonappropriated funds are funds received from sources other than congressional appropriations.

⁹ As required by the March 1, 1999, policy memorandum, the Langley Exchange obtained the FY 1999 audit in accordance with GAS.

Exchange Council Corrective Actions

In response to the audit firm’s findings and recommendations, the Langley Exchange Council documented the Exchange’s status as an instrumentality of the U.S. Government and its compliance with NPD 9050.6E, “NASA Exchange Activities.” The Directive allows Centers to use appropriated¹⁰ funds to provide facilities and equipment for use by the Exchanges. Therefore, the Langley Exchange Council and the Langley Chief Financial Officer consider accounting for the value of the space and utilities provided by the Center unnecessary. Eggleston Smith concurred with the Langley Exchange representations and considers this issue resolved. In addition, the Langley Exchange has initiated plans and/or taken corrective actions to (1) facilitate the reconciliation of ticket sales and purchases to the general ledger and (2) stop backdating checks. We consider the Council’s actions responsive to recommendations.

¹⁰ Appropriated funds are Federal funds authorized (that is, appropriated) by Congress for an agency’s operations. As required by the United States Code, appropriated funds may be used only for their intended purpose and only for a specified period.

Appendix A. Objectives, Scope, and Methodology

Objectives

The quality control review objective was to determine whether the audit work for the Langley Exchange was performed in accordance with applicable auditing standards. We also determined whether the Langley Exchange has taken corrective actions in response to recommendations resulting from the audit.

Scope and Methodology

In performing the quality control review, we used an internal work program that incorporates the auditing standards issued by the AICPA. Based on those standards, we developed and organized the work program according to the general, field work, and reporting standards for financial audits. Our review focused on the auditors' qualifications, independence, peer review report, audit programs for appropriate procedures, and working paper documentation to include the results of the control risk assessment,¹¹ fraud risk assessment,¹² and controls testing. We also reviewed assessments of plans and actions taken by the Langley Exchange to implement the auditors' recommendations.

We performed the quality control review in December 1999.

¹¹ According to AICPA Codification of Statements on Auditing Standards, Section 319, "Consideration of Internal Control in a Financial Statement," auditors are required to document the basis for concluding that control risk is below the maximum level.

¹² AICPA Codification of Statements on Auditing Standards, Section 316, "Fraud in a Financial Statement Audit," states that auditors are required to specifically assess the risk of material misstatement of the financial statements due to fraud and to document in the working papers evidence of its assessment.

Appendix B. Report Distribution

Independent Audit Firm

Eggleston Smith P.C.
Certified Public Accountants and Consultants
603 Pilot House Drive, Suite 400
Newport News, VA 23606

National Aeronautics and Space Administration (NASA) Headquarters

Code B/Chief Financial Officer
Code B/Comptroller
Code BF/Director, Financial Management Division
Code G/General Counsel
Code JL, Director, Contractor Industrial Relations
Code JM/Director, Management Assessment Division

NASA Centers

Chairman, Exchange Council, Langley Space Center
Chief Counsel, John F. Kennedy Space Center

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: Eggleston Smith P.C. Audit of NASA Langley Research Center Exchange Financial Statements for Fiscal Year Ended September 30, 1998

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

NASA Employee

Private Citizen

Government: _____ Federal: _____ State: _____ Local: _____

Media

Public Interest

Other: _____

May we contact you about your comments?

Yes: _____

No: _____

Name: _____

Telephone: _____

Thank you for your cooperation in completing this survey.

Major Contributors to This Report

Patrick A. Iler, Director, Audit Quality

Bonnie Armstrong, Auditor-in-Charge

Nancy C. Cipolla, Report Process Manager