

JANUARY 17, 2007

QUALITY CONTROL REVIEW REPORT

OFFICE OF AUDITS

QUALITY CONTROL REVIEW OF KPMG LLP AND THE
DEFENSE CONTRACT AUDIT AGENCY OFFICE OF
MANAGEMENT AND BUDGET CIRCULAR A-133 AUDITS
OF THE SMITHSONIAN INSTITUTION FOR FISCAL YEAR
ENDED SEPTEMBER 30, 2004

OFFICE OF INSPECTOR GENERAL



National Aeronautics and
Space Administration

REPORT No. IG-07-001 (ASSIGNMENT No. A-06-020-00)

Acronyms

AICPA	American Institute of Certified Public Accountants
CFDA	Catalog of Federal Domestic Assistance
DCAA	Defense Contract Audit Agency
DoD	Department of Defense
FY	Fiscal Year
GAGAS	Generally Accepted Government Auditing Standards
OIG	Office of Inspector General
OMB	Office of Management and Budget

National Aeronautics and
Space Administration

Office of Inspector General
Washington, DC 20546-0001



January 17, 2007

Ms. Ellen Harrison, Partner
KPMG LLP

Mr. John Gay, Boston Branch Manager
Defense Contract Audit Agency

Mr. Terry Craig, Chesapeake Bay Branch Manager
Defense Contract Audit Agency

Mr. Andrew Zino, Comptroller
Smithsonian Institution

SUBJECT: Quality Control Review of KPMG LLP and the Defense Contract Audit Agency Office of Management and Budget Circular A-133 Audits of the Smithsonian Institution for Fiscal Year Ended September 30, 2004 (Assignment No. A-06-020-00)

We are providing this report for your information and use. The audit firm of KPMG LLP and the Defense Contract Audit Agency (DCAA) performed single audits of the Smithsonian Institution (Smithsonian) for the fiscal year (FY) ended September 30, 2004 (FY 2004).¹ Office of Management and Budget (OMB) Circular A-133, "Audits of States, Local Governments, and Non-Profit Organizations," requires these audits.

Background. The Smithsonian, created by an act of Congress in 1846, is a museum, education, and research complex consisting of 16 museums and galleries, the National Zoological Park, and other research facilities. It is based in Washington, D.C., but also maintains facilities and operates programs in five states and Panama. A substantial portion of the Smithsonian's operations is funded from annual Federal appropriations. In addition to Federal appropriations, the Smithsonian receives private support, Government grants and contracts, and earns income from investments and its various business activities. Such business activities include Smithsonian magazines and other publications, a mail-order catalog, and museum shops and food services. The Smithsonian reported total Federal expenditures for FY 2004 of \$105.9 million. The

¹ The specific audit responsibilities were determined through an agreement between KPMG and DCAA. Those responsibilities are listed in Enclosures 2 and 3.

Schedule of Expenditures of Federal Awards² identifies NASA as the funding agency for \$83.8 million (79 percent) of the expenditures.

Quality Control Review Objectives. As the cognizant audit agency for the Smithsonian, the NASA Office of Inspector General (OIG) performed a quality control review of the KPMG and DCAA audits of the Smithsonian for FY 2004.³ The objectives of our quality control review were to determine whether KPMG and DCAA conducted audits in accordance with generally accepted government auditing standards (GAGAS) and the auditing and reporting requirements of OMB Circular A-133 and its related Compliance Supplement (the Supplement). OMB issued the Supplement to assist auditors in meeting the requirements of OMB Circular A-133. Enclosure 1 contains details of the scope and methodology of our review, requirements for single audits, prior quality control reviews, and the latest peer reviews of KPMG and DCAA. Enclosures 2 and 3 contain the results of the audits of the Smithsonian for FY 2004 performed by KPMG and DCAA, respectively.

Review Results. KPMG's and DCAA's audit work met the applicable GAGAS standards and OMB Circular A-133 reporting requirements with the following minor exceptions:

- The Catalog of Federal Domestic Assistance (CFDA) titles and numbers were either missing or were incorrect in the KPMG and DCAA audit reports, the Schedule of Expenditures of Federal Awards, and the data collection form (Finding A).
- KPMG incorrectly documented the Smithsonian as a low-risk auditee on the data collection form (Finding B).
- DCAA's audit, "Report on Smithsonian Astrophysical Observatory's Compliance with Requirements Applicable to its Research and Development Program and on Internal Control Over Compliance in Accordance with OMB Circular A-133, Fiscal Year 2004," was not available on the Federal Audit Clearinghouse's Image Management System (Finding C).

Management Comments. Our draft report made six recommendations to improve future audits of the Smithsonian. We made recommendations to Smithsonian, KPMG, and DCAA to include CFDA titles and numbers and correct auditee risk designations in report documents, and to ensure that audit reports are made available on the Federal Audit Clearinghouse's Image Management System. Smithsonian, KPMG, and DCAA took corrective actions that met the intent of our recommendations, and we consider them closed. See Enclosure 4 for the full text of the comments.

² The Schedule of Expenditures of Federal Awards shows the amount of annual Federal award expenditures by Federal agency.

³ The KPMG office in Washington, D.C., and the DCAA branch offices in Boston, Massachusetts, and Columbia, Maryland, performed the single audits of the Smithsonian for FY 2004.

Finding A

Incorrect or No CFDA Titles and Numbers Provided in Documents. The KPMG and DCAA audit reports, Smithsonian's Schedule of Expenditures of Federal Awards, and the KPMG data collection form for the Smithsonian audit, all either did not contain the CFDA titles and numbers or contained incorrect CFDA data.

OMB Circular A-133 requires the auditee to submit to the Federal Audit Clearinghouse a complete reporting package on each single audit that includes

- the auditor's report;
- a Schedule of Expenditures of Federal Awards; and
- a data collection form certified by the auditee and auditor that the audit was completed in accordance with the Circular.

OMB Circular A-133, section 510(b), states that "Federal program and specific Federal award identification including the CFDA title and number" shall be included, as applicable, in audit findings. In addition, section 310(b) states that at a minimum, the Schedule of Expenditures of Federal Awards shall, "Provide total Federal awards expended for each individual Federal program and the CFDA number or other identifying number when the CFDA information is not available." Finally, section 320(b)(2) states that the data collection form shall include the CFDA number for each Federal program, as applicable.

Our review disclosed that

- the KPMG and DCAA auditors did not include the CFDA titles and numbers in the Federal findings of their audit reports of the Smithsonian,
- the Smithsonian did not list the CFDA numbers in the Schedule of Expenditures of Federal Awards, and
- the Smithsonian's data collection form contained incorrect CFDA number extensions and did not list the names of Federal programs.

The primary purpose of the CFDA number is to assist users in identifying programs that meet specific objectives of the potential applicant and to obtain general information on Federal assistance programs. The CFDA number also helps in coordination and communication between the Federal Government and state and local governments. Without the correct CFDA number extensions or names of Federal programs, Federal users and the public have no referenced source to identify and locate the Federal program using the CFDA Program Index.

Recommendation 1. KPMG should revise the September 30, 2004, data collection form to indicate the CFDA number extensions and the names of Federal programs and include CFDA titles and numbers in the Federal findings in future audit reports of the Smithsonian.

Management's Response. KPMG management acknowledged that its findings did not contain specific CFDA titles and numbers but believes sufficient information was provided to meet the requirements of A-133. KPMG stated that it would work with the Smithsonian to provide the CFDA information in future reports.

Evaluation of Management's Comments. KPMG's action is responsive to the recommendation and the recommendation is closed.

Recommendation 2. The Smithsonian should submit the revised data collection form containing the CFDA number extensions to the Clearinghouse and include the CFDA numbers in the Schedule of Expenditures of Federal Awards in future audits of the Smithsonian.

Management's Response. Smithsonian management stated that many of the sponsored projects listed in the FY 2004 Schedule of Expenditures of Federal Awards were no longer active and, therefore, attempting to pursue the CFDA numbers for the FY 2004 data collection form would not be prudent. Smithsonian management stated that it would obtain CFDA numbers for the FY 2006 and subsequent audits.

Evaluation of Management's Response. Smithsonian's action is responsive to the recommendation and the recommendation is closed.

Recommendation 3. DCAA should include CFDA titles and numbers in the Schedule of Findings and Questioned Costs in future audit reports of the Smithsonian.

Management's Response. DCAA management stated that when audit findings are related to specific awards, DCAA agrees to include the CFDA number in the report. In the case of the FY 2004 report, the reported findings pertained to internal control issues at the Smithsonian, which impacted all Federal awards. As a result, it was not practical to record all of the CFDA numbers.

Evaluation of Management's Response. We agree with DCAA's response and consider the recommendation closed.

Finding B

Incorrect Auditee Risk Designation. The data collection form for the Smithsonian contained the wrong auditee risk designation. KPMG determined and reported in the schedule of findings and questioned costs that the Smithsonian is a high-risk auditee, but the data collection form erroneously stated that the Smithsonian was a low-risk auditee. According to OMB Circular A-133, section 505, the auditor's report should include a

schedule of findings and questioned costs along with a statement regarding whether the auditee qualified as a low-risk auditee. The schedule should be provided in the auditor's report and submitted to the Federal Audit Clearinghouse. OMB Circular A-133, section 320, also requires the auditee to submit a data collection form that states whether the auditee qualified as a low-risk auditee. Because of the inconsistent treatment, Federal users and the public may be uncertain about whether the Smithsonian qualified as a low-risk auditee or a high-risk auditee. Consequently, these users may rely on the low-risk auditee determination indicated on the data collection form without reading the audit report.

Recommendation 4. KPMG should revise the September 30, 2004, data collection form to indicate that the Smithsonian was a high-risk auditee and resubmit the form to the Smithsonian.

Management's Response. KPMG concurred that the data collection form incorrectly indicated that the Smithsonian qualified as a low-risk auditee and will correct the form.

Evaluation of Management's Response. KPMG's action is responsive to the recommendation and the recommendation is closed.

Recommendation 5. The Smithsonian should submit the revised data collection form to the Federal Audit Clearinghouse.

Management's Response. Smithsonian management stated that KPMG will appropriately revise the FY 2004 data collection form and the Smithsonian will submit the revised data collection form to the Federal Audit Clearinghouse.

Evaluation of Management's Response. Smithsonian's action is responsive to the recommendation and the recommendation is closed.

Finding C

Report Not Submitted to Federal Audit Clearinghouse. DCAA's audit, "Report on Smithsonian Astrophysical Observatory's Compliance with Requirements Applicable to its Research and Development Program and on Internal Control Over Compliance in Accordance with OMB Circular A-133, Fiscal Year 2004," June 28, 2005, was not available on the Federal Audit Clearinghouse's Image Management System. OMB Circular A-133, section 320(d), requires that all auditees submit the data collection form and a copy of the reporting package to the Federal Audit Clearinghouse. Because it was not submitted, DCAA's report was unavailable for review by Federal users.

Recommendation 6. The Smithsonian should submit DCAA's report to the Federal Audit Clearinghouse for posting to the Image Management System.

Management's Response. Smithsonian management stated that it submitted the DCAA report to the Federal Audit Clearinghouse for posting on November 2, 2006.

Evaluation of Management's Response. Smithsonian's action is responsive to the recommendation, and the recommendation is closed.

We appreciate the courtesies extended to the audit staff. For additional information on this report, please contact Mr. Karl M. Allen, Project Manager, at 202-358-2595. See Enclosure 5 for the report distribution. The review team members are listed inside the back cover of this report.



Evelyn R. Klemstine
Assistant Inspector General for Auditing

5 Enclosures

QUALITY CONTROL REVIEW PROCESS

Scope and Methodology

We conducted a quality control review of the KPMG and DCAA audits of the Smithsonian for FY 2004 and of the resulting reporting package submitted to the Federal Audit Clearinghouse. We performed our review June 21–28, 2006, at the Washington, D.C., office of KPMG; July 24–28, 2006, at the Boston branch office of DCAA; and August 28–29, 2006, at the Chesapeake Bay branch office of DCAA in Columbia, Maryland. For FY 2004, the Smithsonian reported total Federal expenditures of \$105.9 million, of which \$83.8 million was attributable to NASA.

As the cognizant audit agency responsible for performing the review as part of the project, we focused the review on six areas:

- reporting,
- auditor qualifications,
- planning,
- conduct of the audit work,
- audit work relating to the Schedule of Federal Awards, and
- supervision.

In conducting our review, we assessed the audit documentation prepared by KPMG and DCAA. We also discussed the audit with KPMG and DCAA audit personnel. We emphasized the areas that are of major concern to the Federal Government, such as determining and auditing major program compliance and internal controls.

Single Audit Requirements

The Single Audit Act and OMB Circular A-133 are designed to improve the financial management of state and local governments and nonprofit organizations. The Act and OMB Circular A-133 establish uniform auditing and reporting requirements for all Federal award recipients who are required to obtain a single audit. OMB Circular A-133 establishes policies that guide implementation of the Act and provide an administrative foundation for uniform requirements of non-Federal entities administering Federal awards. OMB Circular A-133 applies to all Federal departments and agencies making awards to non-Federal entities. Entities that expend \$500,000 or more of Federal awards in a fiscal year are subject to the Act and the audit requirements in OMB Circular A-133 and, therefore, must have an annual single or program-specific audit performed in accordance with GAGAS. To meet the requirements of the Act and OMB Circular

A-133, the auditee submits to the Federal Audit Clearinghouse a complete reporting package on each single audit. The submission includes the following:

- a data collection form certified by the auditee and auditor that the audit was completed in accordance with the Circular;
- financial statements and related opinions;
- a Schedule of Expenditures of Federal Awards and related opinion;
- a report on compliance and internal controls over financial reporting;
- a report on internal control over compliance for major programs;
- a report on compliance with requirements for major programs and related opinions;
- a schedule of findings and questioned costs;
- a summary schedule of prior audit findings, when appropriate; and
- a corrective action plan, when appropriate.

The Supplement assists auditors in identifying the compliance requirements that the Federal Government expects to be considered as part of the single audit. For each compliance requirement, the Supplement describes the related audit objectives for the auditor to consider in each audit conducted in compliance with OMB Circular A-133 and also suggests audit procedures. The Supplement also describes the objectives of internal controls and characteristics that, when present and operating effectively, help ensure compliance with requirements. The following 14 compliance requirements identified in the Supplement may be material to a major program that is 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 American Institute of Certified Public Accountants (AICPA) Audit Guide provides guidance on auditor responsibilities for conducting audits according to the Act and OMB Circular A-133. In general, the Audit Guide provides auditors with an understanding of the unique planning, performance, and reporting considerations for single audits performed in compliance with GAGAS. In addition, the Audit Guide uses summary tables and detailed discussions to provide the auditor with an understanding of the

additional GAGAS general, fieldwork, and reporting requirements, including the additional standards relating to quality control systems, continuing professional education, working papers, audit follow-up, and reporting.

The AICPA Audit Guide emphasizes that when planning an audit to meet the requirements of OMB Circular A-133, several factors should be considered in addition to those ordinarily associated with an audit of financial statements in accordance with generally accepted auditing standards and GAGAS. The factors include, but are not limited to, the following:

- determining that the Schedule of Expenditures of Federal Awards is presented fairly in relation to the financial statements taken as a whole;
- determining major programs for audit using a risk-based approach;
- determining compliance requirements;
- gaining an understanding of internal controls over compliance for major Federal programs;
- testing internal controls over compliance for major programs;
- determining compliance with laws, regulations, and the provisions of contract or grant agreements that have a direct and material affect on each major program; and
- satisfying the additional requirements of the Act and OMB Circular A-133 for working papers, audit follow-up, and reporting.

Prior Quality Control Reviews

On November 16, 2000, we issued a “Quality Control Review of KPMG LLP and Defense Contract Audit Agency Audit of Smithsonian Institution for Fiscal Year Ended September 30, 1999” (IG-01-004). During the 2000 review, we determined that the KPMG audit work and report met the applicable auditing and reporting guidance and regulatory requirements contained in OMB Circular A-133 and GAGAS. However, we found that in the 1999 review, DCAA did not meet the auditing requirements of OMB Circular A-133 and GAGAS in several areas. Specifically, the DCAA auditors did not

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

We recommended that DCAA document working papers to adequately describe the auditor’s understanding of internal controls and the planned and completed internal control testing for current and future audits. We also recommended that DCAA test

internal controls and audit the procurement compliance requirement in accordance with OMB Circular A-133.

DCAA responded that it improved the internal control documentation by including additional working papers and references and that it planned to conduct staff training on the requirements for adequate working paper documentation. DCAA also agreed to improve control testing documentation for the FY 1999 audit and revise the working papers to reflect the status of the Smithsonian's compliance with suspension and debarment activities, a key element in the validation of the procurement system.

PricewaterhouseCoopers Peer Review of KPMG

We reviewed the March 1, 2006, peer review report on KPMG by PricewaterhouseCoopers to determine whether we needed to be aware of any issues during our report and working paper review. PricewaterhouseCoopers determined that KPMG met the requirements of the quality control review standards established by the AICPA and that KPMG complied with the standards during the fiscal year ended March 31, 2005.

In addition to the peer review peer review report, PricewaterhouseCoopers issued a letter on March 1, 2006, that sets forth comments relating to certain policies and procedures or compliance with them. According to the letter, PricewaterhouseCoopers noted that KPMG did not consistently follow its policy of ensuring that the use of "internal specialists" (e.g., tax specialists and information technology specialists) is appropriately coordinated to ensure that the work of the specialist is properly integrated into the overall audit process. PricewaterhouseCoopers also commented that KPMG's internal inspection found noncompliance with policies requiring working papers to capture the procedures performed and conclusions reached on each engagement, instances where items within the financial statements were misclassified, and required disclosures that were omitted or incomplete. PricewaterhouseCoopers recommended that KPMG provide additional training for professionals performing employee benefit plan audits, enhance guidance for testing claim payments in health and welfare plans, and compile and maintain a national inventory of its employee benefit plan engagements to effectively monitor the practice. We determined that the above issues were not of sufficient significance to affect our review of the KPMG working papers and report.

Department of Defense OIG Peer Review of DCAA

We reviewed the December 15, 2003, peer review report on DCAA, performed by the Department of Defense (DoD) OIG. The DoD OIG reviewed the DCAA audit operation's system of quality control for the 3-year period ending September 30, 2002, and issued an unqualified opinion.

DoD OIG also issued a separate Memorandum of Comments and Observations on December 15, 2003, noting that DCAA did not adequately plan and perform the review of internal controls over compliance requirements for major Federal programs for single audits. The DCAA agreed that continued diligence in the area of single audits was necessary.

The DoD OIG also noted that DCAA did not perform any independent testing to determine whether it was complying with various requirements specified in the qualification and independence standards. DCAA stated that the DoD OIG did not convey that the Quality Assurance organization's efforts included documenting the monitoring and testing of other DCAA oversight organizations, which are also key elements of DCAA's overall quality control system. To make the most effective use of existing agency resources, DCAA stated that its system of quality control is designed to rely on the oversight performed by other Headquarters elements, not duplicate it. DCAA agreed that monitoring and testing by other Headquarters oversight elements, as well as DCAA's Quality Assurance organization, should be expanded to better cover selected areas pointed out by the DoD OIG. However, DCAA did not agree that DCAA's Quality Assurance organization needs to substantially re-test all monitoring and initial testing that is more appropriately done by other DCAA oversight elements.

During its initial review, the DoD OIG determined that DCAA did not track the requirement that 24 hours of the required 80 continuing professional education hours be in a subject directly related to Government environment and to Government auditing. DCAA stated that the 24-hour continuing professional education requirement has always been part of DCAA's audit policy and clearly documented the requirement in Chapter 21, "Training and Development," of the DCAA Personnel Management Manual. DCAA concurred, however, and also incorporated this requirement into the DCAA's Contract Audit Manual.

The DoD OIG also determined that the DCAA ethics program needed greater emphasis and visibility to ensure that all employees understood the requirements of the various laws and regulations related to ethical behavior. DCAA has corrected these ethics program deficiencies. In our opinion, these issues were not of sufficient significance to affect our review of the DCAA working papers and report.

RESULTS OF THE KPMG AUDIT OF THE SMITHSONIAN INSTITUTION FOR FY 2004

KPMG Audit Report

On December 22, 2004, KPMG issued its report on the financial statements and its report on internal controls for the Smithsonian. On April 22, 2005, KPMG issued its report on compliance for the Smithsonian. The KPMG auditors were responsible for auditing the Smithsonian's financial statements and the following compliance requirements for the Research and Development major program: cash management; Davis-Bacon Act; matching, level of effort, earmarking; program income; real property acquisition and relocation assistance; and reporting.

The KPMG auditors issued an unqualified opinion⁴ on the financial statements, Schedule of Expenditures of Federal Awards, and major program compliance, and noted no matters involving internal controls relating to the financial statements or the major program that were considered material weaknesses.⁵ KPMG identified \$274,422 in questioned costs and reported four findings related to Federal awards as follows:

- **Allowable Costs - Non-Payroll Related Costs.** KPMG determined that the Smithsonian made stipend payments of \$130,688 to individuals working on a grant. Stipend payments were not allowable under the grant agreement.
- **Matching, Level of Effort, Earmarking.** KPMG noted that the Smithsonian did not have a standard process to review amounts used to satisfy cost share requirements. As a result, documentation supporting the composition and original nature of the amounts used to satisfy cost share requirements was not readily available.
- **Allowable Costs - Payroll Costs.** KPMG questioned \$143,567 in salaries and related fringe benefits paid to employees who did not prepare timesheets.

⁴ An unqualified opinion means that the financial statements present fairly, in all material respects, financial position, results of operations, and cash flows in conformity with generally accepted accounting principles.

⁵ The AICPA Audit Guide, May 1, 2003, Appendix D, defines a material weakness as a condition in which the design or operation of one or more of the internal control components 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.

- **Allowable Costs - Fringe Benefits.** KPMG noted one case involving \$167 in annual leave that was charged to only one project when the individual was working on four projects.

KPMG's report was made available to NASA, as well as all other Federal agencies that provided funding to the Smithsonian, by way of the Federal Audit Clearinghouse. We are not aware of any specific action taken by NASA in response to KPMG's findings.

RESULTS OF THE DCAA AUDIT OF THE SMITHSONIAN INSTITUTION FOR FY 2004

DCAA Audit Reports

“Report on Smithsonian Astrophysical Observatory’s Compliance with Requirements Applicable to its Research and Development Program and on Internal Control Over Compliance in Accordance with OMB Circular A-133, Fiscal Year 2004,” June 28, 2005. The DCAA Boston Branch Office performed this audit.

The DCAA auditors were responsible for auditing the following compliance requirements for Smithsonian’s Astrophysical Observatory: activities allowed or unallowed, allowable costs/cost principles, eligibility, equipment and real property management, period of availability of Federal funds, procurement suspension and debarment, subrecipient monitoring, and special tests and provisions. The DCAA auditors issued a qualified opinion⁶ on major program compliance and identified no material weaknesses or reportable conditions. DCAA qualified its opinion on major program compliance because assist audit requests of subcontractor costs totaling \$10,121,834 were not received in time to incorporate into its report.

“Report on Smithsonian Institution (SI Mall Based) Compliance with Requirements Applicable to the Major Programs and on Internal Control Over Compliance in Accordance with OMB Circular A-133, FY 2004,” June 28, 2005. The DCAA

Chesapeake Bay Branch Office in Columbia, Maryland, performed this audit. The DCAA auditors were responsible for auditing indirect costs of the Smithsonian’s mall-based operations for the following three compliance requirements: activities allowed or unallowed, allowable costs/cost principles, and period of availability of funds. The DCAA auditors issued an unqualified opinion on major program compliance, identified no material weaknesses in internal controls over major program, and identified three reportable conditions related to internal controls over compliance as noted below.

- **Period of Availability of Federal Funds.** DCAA determined that two sampled transactions that were related to FY 2003 were incorrectly posted to the FY 2004 period.
- **Activities Allowed or Unallowed.** DCAA determine that two employees did not have proper authority/responsibility checked on their security access forms, and three employees did not have the delegation amount pertaining to the purchasing process, stated on their security access forms.

⁶ A qualified opinion means that except for the effects of the matter to which a qualification relates the financial statements fairly present financial position, results of operations, cash flows, in conformity with generally accepted accounting principles.

- **Allowable Costs/Cost Principles.** DCAA determined that one of Smithsonian's remote units, Smithsonian Tropical Research Institute, had applied the incorrect fringe benefit rate to awards under that unit's responsibility.
- **Period of Availability of Federal Funds.** DCAA determined that the Smithsonian's accounting system did not have effective controls in place to prevent the posting of costs to cost objectives that have been closed out in prior periods.



Evelyn R. Klemstine
Assistant Inspector General for Auditing
Office of Inspector General
NASA
December 20, 2006
Page 2

Paragraph 7.10 of the Audit Guide states "The auditors may be unable to obtain the CFDA number, which is sometimes the case for new federal programs and R&D programs. In addition, cost-type contracts normally will not have a CFDA number. When the CFDA number is not available, the auditee has alternatives for presenting that information. The auditee could indicate that the CFDA number is not available and include, if available, another identifying number, such as a contract or grant number." KPMG presented the major program name and the specific award or contract number for audit findings 2004-1 thru 2004-3 and the major program name for audit finding 2004-4. A specific award or contract number was not presented for finding 2004-4 since the finding was not related to a specific grant or program but to all Mall-based Research and Development programs.

In summary we acknowledge our findings did not contain specific CFDA titles and numbers. We appreciate the importance of findings containing specific information to enable the federal awarding agency and the entities to fulfill their follow up responsibilities. The engagement team believes that sufficient information was provided to fulfill these responsibilities. However, the engagement team will work with the Smithsonian to provide the cited information in future reports.

Matter 2

The Schedule of Expenditures of Federal Awards (SEFA) is the auditee responsibility and your finding regarding CFDA numbers does not involve an error that results in a misstatement that renders the SEFA to be not fairly stated in all material respects.

Finding B

We concur that the data collection form incorrectly indicated that the Smithsonian qualified as a low risk auditee. We are prepared to correct the revised data collection form once NASA and Smithsonian reach a mutual understanding as to whether 2004 data collection form will be revised to include CFDA number extensions.

#2778 2.002/003

KPMG

DEC 20 2006 15:46



Evelyn R. Klemstine
Assistant Inspector General for Auditing
Office of Inspector General
NASA
December 20, 2006
Page 3

Finding C - Did not apply to KPMG.

Because your opinion matters to KPMG and our quality control, we want to make sure that our interpretation and application of the A-133 requirements is appropriate. We thank you in advance for your attention to our position on these matters and look forward to further discussions with you.

Very truly yours,

Ellen Harrison
Partner

#2776 P.003/003

KPMG

DEC.20.2006 15:47



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 (A-06-020-00)

November 24, 2006

Ms. Evelyn R. Klemstine
Assistant Inspector General for Audit
Attention: Ms. Catherine Schneider, Financial and Institutional Management Director
NASA Headquarters, Office of Inspector General,
300 E. Street, SW
Washington DC, 20546

SUBJECT: DCAA Comments on Draft NASA IG Report on the Quality Control Review of
KPMG LLP and the Defense Contract Audit Agency Office of Management And
Budget (OMB) Circular A-133 Audits of the Smithsonian Institution for Fiscal Year
Ended September 30, 2004 (Assignment No. A-06-020-00)

Dear Ms. Schneider:

Thank you for the opportunity to respond to the draft report. The subject report provides the results of your office's quality control review of the OMB Circular A-133 audit performed at the Smithsonian Institution for Fiscal Year 2004. Our detailed response to the report recommendation is contained in the attached memorandum from the DCAA Mid Atlantic Regional Office.

As discussed in the DCAA Mid-Atlantic Regional Office's response, DCAA concurs that the Catalog of Federal Domestic Assistance (CFDA) titles and numbers should be included in DCAA audit reports, when applicable. However, we believe Audit Report No. 6171-2004S10110001 is in compliance with OMB Circular A-133. The audit findings in the subject DCAA audit report pertain to internal control issues at the Smithsonian Institution. These internal control issues are not identified to specific Federal awards. Therefore, in our opinion, it would not be appropriate or relevant to include a specific CFDA number in the audit report notes when the audit findings reported are not identified with a specific Federal award or CFDA number. OMB Circular A-133, Appendix B, section .510, Audit Findings, requires that specific information be included, as applicable, in audit findings. Section 510(b)(1) further states "When information, such as the CFDA title and number or Federal award number, is not available, the auditor shall provide the best information available to describe the Federal award." The audit report did contain a listing of grant awards. If the audit findings related to specific awards, we would include the applicable CFDA number, if provided by the contractor, in our Schedule of Findings and Questioned Costs.

PQA 225.4 (A-06-020-00) November 24, 2006
SUBJECT: DCAA Comments on Draft NASA IG Report on the Quality Control Review of
KPMG LLP and the Defense Contract Audit Agency Office of Management And
Budget Circular A-133 Audits of the Smithsonian Institution for Fiscal Year Ended
September 30, 2004 (Assignment No. A-06-020-00)

If you have any questions, please contact Ms. Mary L. Silva, Chief, Policy Quality
Assurance Division, at (703) 767-3439 or Ms. Deaune Volk, Policy Quality Assurance Division,
at (703) 767-2285.

Sincerely,



Kenneth J. Saccoccia
Assistant Director
Policy and Plans

Enclosure:
Mid-Atlantic Region Response dated November 24, 2006



MAR Regional
Response to NASA IG

Copy Furnished:
RQA-6, 6171



IN REPLY REFER TO

**CHESAPEAKE BAY BRANCH OFFICE
MID-ATLANTIC REGION
DEFENSE CONTRACT AUDIT AGENCY
DEPARTMENT OF DEFENSE**

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Columbia, Maryland 21044-3329
410-964-2070
410-997-0509 (FAX)
DCAA-FAO6171@dcaa.mil

820.1/617

November 24, 2006

MEMORANDUM FOR REGIONAL DIRECTOR, MID-ATLANTIC REGION, DCAA

ATTENTION: RQA-6, Mr. Art Ruggia

SUBJECT: Response to Discussion Draft Report on the Quality Control Review of KPMG LLP and the Defense Contract Audit Agency Office of Management and Budget Circular A-133 Audit of the Smithsonian Institution for Fiscal Year Ended September 30, 2004 (Project No. A-06-020-00)

Thank you for the opportunity to respond to the draft report and the results of the evaluation reported therein. Our response to Finding A (i.e., Incorrect or no Catalog of Federal Domestic Assistance (CFDA) Titles and Numbers provided in Documents) applicable to the Defense Contract Audit Agency Audit Report No. 6171-2004S10110001 is as follows:

Reviewer Comment: The DCAA audit report did not contain the CFDA titles and numbers. DCAA should include the CFDA titles and numbers in the Schedule of Findings and Questioned Costs in future audit reports of the Smithsonian (recommendation 3).

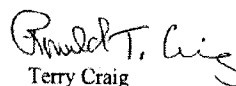
DCAA Response: We believe Audit Report No. 6171-2004S10110001 is in compliance with OMB Circular A-133. OMB Circular A-133, Appendix B, Section .510, *Audit Findings* requires that specific information be included, as applicable, in audit findings. Section 510(b)(1) further states "When information, such as the CFDA title and number or Federal award number, is not available, the auditor shall provide the best information available to describe the Federal award."

When the audit findings are related to specific awards, DCAA agrees to include the affected award number in the report notes, if the CFDA information is provided by the contractor. However, the OMB Circular A-133 audit findings reported in the DCAA Chesapeake Bay Branch Office A-133 audit report (6171-2004S10110001) do not pertain to a specific award. The audit report findings pertain to internal control issues at the Smithsonian Institution, which impact all federal awards at the contractor. In addition, the CFDA numbers were not provided by the contractor. When information, such as the CFDA title and number or Federal award number is not available, DCAA will provide the best information available to describe the Federal award.

6171 820.1

SUBJECT: Response to Discussion Draft Report on the Quality Control Review of KPMG LLP and the Defense Contract Audit Agency Office of Management and Budget Circular A-133 Audits of the Smithsonian Institution for Fiscal Year Ended September 30, 2004 (Project No. A-06-020-00)

Questions regarding this memorandum should be directed to Mr. Terry Craig, Branch Manager, at (410) 964-2231.



Terry Craig
Branch Manager
Chesapeake Bay Branch Office

CC:
RAMD-6



Smithsonian Institution

Comptroller

November 15, 2006

Ms. Evelyn R. Klemstine
Assistant Inspector General for Auditing
National Aeronautics and Space Administration
Washington, DC 20546-0001

RE: Quality Control Review of KPMG LLP and the Defense Contract Audit Agency
Office of Management and Budget Circular A-133 Audits of the Smithsonian Institution
for Fiscal Year Ended September 30, 2004 (Assignment No. A-06-020-00)

Dear Ms. Klemstine:

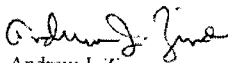
This is in response to your October 18, 2006 request for comments on the subject audit report and an indication of what actions the Smithsonian Institution will take in response to the report recommendations.

The Smithsonian finds the report technically accurate. Comments and actions to be taken in response to the report recommendations are in the Enclosure.

Thank you for the opportunity to comment on the draft audit report

If you have any questions, please contact Charles Crichley of my staff at (202) 275-0673.

Sincerely,


Andrew J. Zino

Enclosure

cc
KPMG LLP
DCAA Chesapeake Bay Branch Office
DCAA Boston Branch Office

Smithsonian Institution
Office of Sponsored Projects
Comments on NASA Quality Review Recommendations
November 2006

Finding A: Incorrect or No CFDA Titles and Numbers Provided in Documents

Recommendation 2: The Smithsonian should submit the revised data collection form containing the CFDA number extensions to the Clearinghouse and include the CFDA numbers in the Schedule of Expenditures of Federal Awards in future audits of the Smithsonian.

Smithsonian Comment and Planned Corrective Action: Federal sponsors frequently fail to provide CFDA numbers in award documents. The Smithsonian policy has been to handle CFDA inquires on a case-by-case basis, and there have been no CFDA inquires related to fiscal year 2004. Many of the sponsored projects listed in the fiscal year 2004 Schedule of Expenditures of Federal Awards are no longer active. In the circumstances, attempting to identify the active projects and pursuing CFDA numbers is not considered prudent. The Smithsonian will obtain CFDA numbers for fiscal year 2006 and subsequent federal awards and include them on the Schedule of Expenditures of Federal Awards.

Finding B: Incorrect Auditee Risk Designation

Recommendations 4 and 5: KPMG should revise the September 30, 2004 data collection form to indicate that the Smithsonian was a high-risk auditee and resubmit the form to the Smithsonian. The Smithsonian should submit the revised data collection form to the Federal Audit Clearinghouse.

Smithsonian Comment and Planned Corrective Action: KPMG has informed the Smithsonian that it will revise the September 30, 2004 data collection form to indicate that the Smithsonian was a high-risk auditee. The Smithsonian will submit the revised data collection form to the Federal Audit Clearinghouse.

Finding C: Report Not Submitted to Federal Audit Clearinghouse:

Recommendation 6: The Smithsonian should submit DCAA's report to the Federal Audit Clearinghouse for posting to the Image Management System.

Smithsonian Comment and Planned Corrective Action: The DCAA report was submitted to the Federal Audit Clearinghouse for posting on November 2, 2006.

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REPORT DISTRIBUTION

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Mr. Peter Meade, Non Profit Technical Specialist
Mr. Kenneth Saccoccia, Assistant Director, Policy and Plans

Audited Organization

Mr. Andrew Zino, Comptroller, The Smithsonian Institution

Federal Offices of Inspector General

Agency for International Development
Department of Agriculture
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Deputy Associate Director, Energy and Science Division
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Federal Audit Clearinghouse

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Senate Committee on Appropriations
Senate Subcommittee on Commerce, Justice, and Science
Senate Committee on Commerce, Science, and Transportation
Senate Subcommittee on Science and Space
Senate Committee on Homeland Security and Government Affairs
House Committee on Appropriations
House Subcommittee on Science, State, Justice, and Commerce
House Committee on Government Reform
House Subcommittee on Government Management, Finance, and Accountability
House Committee on Science
House Subcommittee on Space and Aeronautics

Major Contributors to the Report:

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Karl M. Allen, Project Manager

JANUARY 17, 2007

REPORT No. IG-07-001



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COMMENTS ON THIS REPORT

In order to help us improve the quality of our products, if you wish to comment on the quality or usefulness of this report, please send your comments to Ms. Jacqueline White, Director of Quality Assurance, at Jacqueline.White@nasa.gov or call 202-358-0203.

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
NASA Headquarters
Washington, DC 20546-0001

NASA HOTLINE

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