

IG-02-005

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**QUALITY  
CONTROL  
REVIEW  
REPORT**

**RJ RICCIARDI, CPA, AUDIT OF THE SEARCH  
FOR EXTRATERRESTRIAL INTELLIGENCE  
INSTITUTE, FISCAL YEAR ENDED  
SEPTEMBER 30, 1999**

**December 6, 2001**

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National Aeronautics and  
Space Administration

**OFFICE OF INSPECTOR GENERAL**

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## **Acronyms**

AICPA	American Institute of Certified Public Accountants
GAAP	Generally Accepted Accounting Principles
GAGAS	Generally Accepted Government Auditing Standards
NASA	National Aeronautics and Space Administration
OIG	Office of Inspector General
OMB	Office of Management and Budget
PPC	Practioners Publishing Company
SETI	Search for Extraterrestrial Intelligence
SOP	Statement of Position

W

December 6, 2001

Mr. Ralph J. Ricciardi  
1000 Fourth Street, Suite 725  
San Rafael, CA 94901

Re: Final Quality Control Review Report of RJ Ricciardi, CPA, Audit of the Search for Extraterrestrial Intelligence Institute for the Fiscal Year Ended September 30, 1999, Assignment No. A-01-025-00  
Report Number IG-02-005

Dear Mr. Ricciardi:

The subject final report is provided for your use and comment. Please refer to the Executive Summary for the overall review results. Our evaluation of your response is incorporated into the body of the report. Your comments on a draft of this report were responsive to recommendations 1, and 4 through 6, and your completed actions are sufficient to close them for reporting purposes.

Your corrective actions for recommendations 2 and 3 to document internal control were not fully responsive because you did not specifically address corrective actions for the reporting compliance requirement for the current and future years. Your comments on recommendations 7 and 8 also were not fully responsive because you did not address whether future years' audits would comply with the recommended corrective action. Therefore, we ask that you provide additional comments on the final report not later than February 4, 2002. Recommendations 2, 3, 7, and 8 will remain unresolved for reporting purposes.

If you have questions concerning the report, please contact Mr. Chester A. Sipsock, Program Director, Financial Management Audits, Quality, and Oversight, at (216) 433-8960, or Ms. Vera J. Garrant, Auditor-in-Charge, at (202) 358-2596. We appreciate the courtesies extended to the audit staff. The final report distribution is in Appendix H.

Sincerely,

**[original signed by]**

Alan J. Lamoreaux  
Assistant Inspector General for Audits

Enclosure

cc:

AB/Associate Deputy Administrator for Institutions

B/Acting Chief Financial Officer

B/Comptroller

BF/Director, Financial Management Division

G/General Counsel

H/Associate Administrator for Procurement

JM/Director, Management Assessment Division

W

December 6, 2001

Ms. Shannon Atkinson, Chief Financial Officer  
SETI Institute  
2035 Landings Drive  
Mountain View, CA 94043-0818

Re: Final Quality Control Review Report of RJ Ricciardi, CPA, Audit of the Search for  
Extraterrestrial Intelligence Institute for the Fiscal Year Ended September 30, 1999,  
Assignment No. A-01-025-00  
Report Number IG-02-005

Dear Ms. Atkinson:

The subject final report is provided for your use and comment. Please refer to the  
Executive Summary for the overall review results. Our evaluation of your response is  
incorporated into the report. Your comments on a draft of this report were responsive to  
the information in Appendix E.

If you have questions concerning the report, please contact Mr. Chester A. Sipsock,  
Program Director, Financial Management Audits, Quality, and Oversight, at (216) 433-  
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# NASA Office of Inspector General

IG-02-005  
A-01-025-00

December 6, 2001

## RJ Ricciardi, CPA,<sup>1</sup> Audit of the Search for Extraterrestrial Intelligence Institute for the Fiscal Year Ended September 30, 1999

### Introduction

The Search for Extraterrestrial Intelligence (SETI) Institute, Mountain View, California, conducts scientific research and educational projects relevant to the nature, prevalence, and distribution of life in the universe. The Institute also conducts formal and informal science education related to these fields of interest.

The National Aeronautics and Space Administration (NASA) is the oversight agency for audit for the SETI Institute. The NASA Office of Inspector General (OIG) performed a quality control review of the RJ Ricciardi, CPA, audit of the SETI Institute for the fiscal year ended September 30, 1999.<sup>2</sup> The Single Audit Act and the Single Audit Act Amendments<sup>3</sup> require the audit. The SETI Institute reported total NASA expenditures of \$4.6 million and total Federal expenditures of \$5.2 million for fiscal year 1999.

Appendix A provides details on the single audit requirements.

### Objectives

**Audit Report.** The objective of our report quality control review was to determine whether the report that SETI Institute submitted to the Federal Audit Clearinghouse<sup>4</sup> for fiscal year 1999 met applicable reporting standards and Office of Management and Budget (OMB) Circular A-133<sup>5</sup> reporting requirements.

**Audit Working Papers.** The objectives of our audit working paper quality control review were to determine whether RJ Ricciardi, CPA, conducted the audit in accordance

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<sup>1</sup> CPA means certified public accountant.

<sup>2</sup>The San Rafael, California, office of RJ Ricciardi performed the single audit for the SETI Institute fiscal year ended September 30, 1999. We performed a quality control review of the 1999 working papers because Mr. Ricciardi explained that the working papers supporting the fiscal year 2000 audit were not ready to be subject to an external review.

<sup>3</sup>Office of Management and Budget Circular A-133, "Audits of States, Local Governments, and Non-Profit Organizations," implements the requirements of the Single Audit Act and the Single Audit Act Amendments. Appendix A contains details on the requirements of the Circular.

<sup>4</sup>The Single Audit Act Amendments of 1996, §7504(c), require the Office of Management and Budget to establish the Federal Audit Clearinghouse to receive the Circular A-133 audit reports.

<sup>5</sup> See footnote number 2.



with applicable standards and whether the audit met the auditing and reporting requirements of OMB Circular A-133. Appendixes B and C contain details on the objectives, scope, and methodology.

## Results of Review

On December 29, 1999, RJ Ricciardi, CPA, issued its audit report on the SETI Institute for the fiscal year ended September 30, 1999.

- **Reported A-133 Results.** The auditors (1) identified no findings; (2) questioned no costs; and (3) issued an unqualified opinion<sup>6</sup> on the financial statements, Schedule of Expenditures of Federal Awards,<sup>7</sup> and major program compliance. The auditors also found no instances of noncompliance in the financial statement audit that are required to be reported under generally accepted government auditing standards (GAGAS).<sup>8</sup> Finally, the auditors noted no matters involving internal controls relating to the financial statements or the major program that are considered to be material weaknesses.<sup>9</sup>
- **Report Quality Review Results.** The SETI Institute's audit report met the applicable reporting guidance and regulatory requirements in OMB Circular A-133.
- **Audit Quality Review Results.** The RJ Ricciardi, CPA, audit work does not meet the applicable auditing guidance and requirements in (1) OMB Circular A-133 and its related Compliance Supplement,<sup>10</sup> (2) GAGAS, and (3) generally accepted auditing standards. The auditors did not properly plan the audit to meet OMB Circular A-133 audit requirements (Finding A). The auditors also did not audit the period of availability of Federal funds and reporting compliance requirements (Finding B). Finally, the auditors did not adequately document their working papers for their understanding of internal controls related to the activities allowed or unallowed requirement; internal control testing for the equipment, procurement and suspension and debarment, and reporting compliance requirements; and compliance testing for

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<sup>6</sup>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 provisions that could have a direct and material effect on each major program.

<sup>7</sup>The Schedule of Expenditures of Federal Awards shows the amount of annual Federal award expenditures by Federal agency for each program, grant, or contract.

<sup>8</sup>These standards are broad statements of the auditors' responsibilities, promulgated by the Comptroller General of the United States.

<sup>9</sup>The American Institute of Certified Public Accountants (AICPA) Statement of Position 98-3, Appendix D, defines a material weakness as:

... the condition in which the design or operation of one or more of the internal control components [control environment, risk assessment, control activities, information and communication, and monitoring] does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions.

<sup>10</sup> Appendix A contains additional details on the Compliance Supplement.

the cash management compliance requirement. In addition, the auditors did not document their determination of major programs and the low-risk auditee status for the Institute (Finding C).

**Quality Control Review Referral.** Based on the results of our quality control review, we determined that RJ Ricciardi, CPA, audit work meets the President's Council on Integrity and Efficiency's definition of a referable action under the Council's Position Statement 4, "IG [Inspector General] Quality Control Referral Procedures." Therefore, we will refer the staff assigned to this audit to the American Institute of Certified Public Accountants (AICPA). Appendix D contains a definition of a referable action and the rationale for a referral of RJ Ricciardi, CPA.

**Recommendations.** We recommended that for the SETI Institute fiscal year ended September 30, 1999, and for future audits, RJ Ricciardi, CPA:

- Plan the audit of Federal awards to meet OMB Circular A-133 auditing requirements.
- Audit the compliance requirements that have a direct and material effect on the major program, including the period of availability of Federal funds and reporting compliance requirements
- Require auditors to document the working papers (1) for their understanding of the internal controls, internal controls testing, and compliance testing for the compliance requirements (including equipment and cash management) within its audit scope and (2) to support their determination of major programs and the classification of SETI as low risk.

**Management's Response.** The audit firm partially concurred with the recommendation to audit the period of availability of Federal funds requirement. The firm stated that the auditors extensively audited this requirement. The audit firm concurred with the remaining recommendations and emphasized that the audit was planned and executed as an organization-wide audit, which included the financial statements and Federal awards. However, the firm agreed that in some cases, the working paper documentation could be improved. The auditors had prepared a Federal awards planning document, documented the working papers to indicate which of the 14 compliance requirements had a direct and material effect on the major program, documented their understanding and testing of internal control, and prepared additional documentation that identified the compliance testing performed. The audit firm agreed to implement the corrective action on future years' audits. The complete text of the response is in Appendix F.

**Evaluation of Management's Response.** The OMB Circular A-133 reporting package consists of the financial statement audit and the Federal awards audit. Although, these audits have different objectives, their audit procedures may be combined, in some cases, to conduct an efficient audit. Therefore, the working papers must contain sufficient documentation to enable an independent reviewer to understand the procedures performed to meet the objectives of each audit.

We maintain that the auditors neither adequately documented their understanding of internal control for the reporting compliance requirement for the current year's audit nor addressed how they plan to meet the requirement in future years' audits. Also, the audit firm did not address the planned corrective action to document the equipment and cash management compliance requirements in future years' audits. Therefore, we request that the audit firm further review its position on these matters and provide additional comments.

Except as described in the two preceding paragraphs, the completed corrective action for the recommendations in the current year and the planned corrective actions for future years' audits are responsive and are sufficient to close the related recommendations for reporting purposes.

**Other Matters of Interest.** During our report review, we identified issues related to reporting that should be brought to the attention of SETI Institute management. These issues do not affect the results of our review and are discussed in Appendix E. The SETI Institute management agreed to correct these issues in future audit reports. Appendix G contains the complete text of the SETI Institute response.

## **Introduction**

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

A complete reporting submission in accordance with OMB Circular A-133 includes the following: (1) financial statements and related opinion, (2) Schedule of Expenditures of Federal Awards and related opinion, (3) report on internal controls and compliance review on the financial statements, (4) report on internal controls review and compliance opinion on major programs, and (5) Schedule of Findings and Questioned Costs.<sup>11</sup>

Appendix A contains additional details on the Single Audit requirements.

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<sup>11</sup>Appendix C describes the information in the Schedule of Findings and Questioned Costs.

## **Findings and Recommendations**

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### **Finding A. Planning the Audit**

The auditors did not properly plan the OMB Circular A-133 audit to accomplish all the audit objectives. Specifically, the auditors did not adequately plan the audit to ensure that all the compliance requirements that have a direct and material effect on the major program were audited. This occurred because the auditors did not plan the Federal awards audit separately from the financial statement audit. As a result, the audit work was incomplete and Federal agencies and other report users cannot rely on the audit.

#### ***OMB Circular A-133 Audit Requirements***

**General Requirements.** The June 24, 1997, revision of OMB Circular A-133 describes the audit scope in §\_\_.500. In general, the auditors are required to plan the audit to meet the following required internal control and compliance objectives:

- Plan the testing of internal control for each major program to support a low assessed level of control risk for the assertions relevant to the compliance requirements.
- Perform the planned internal control testing.
- Determine whether the audited organization has complied with laws, regulations, and the provisions of contracts or grant agreements that may have a direct and material effect on each of the major programs audited.

**Planning the Internal Control Review.** In general, OMB Circular A-133 §\_\_.500(c)(1) requires the auditor to perform procedures to obtain an understanding of internal controls over Federal programs that is sufficient to plan the audit for major programs; plan the testing of internal control over major programs to support a low assessed level of control risk for the assertions relevant to the compliance requirements for each major program; and unless internal control is likely to be ineffective, perform testing of internal control as planned. AICPA Statement of Position (SOP) 98-3, “Audits of States, Local Governments, and Not-for-Profit Organizations Receiving Federal Awards,” sections 8.7, 8.10, and 8.16, describe the auditors’ responsibilities for planning the review of internal controls for major programs. The auditors must obtain a sufficient understanding of internal control over Federal programs by performing procedures to understand the design of the five elements of internal control (control environment, risk assessment, control activities, information and communication, and monitoring) related to the A-133 compliance requirements for each major program. The auditors must also determine whether the internal controls are operating. The auditors plan the internal

control testing to support a low assessed level of control risk for the assertions<sup>12</sup> relevant to the compliance requirements for each major program. SOP 98-3 section 8.16 explains that:

... Federal agencies want to know if conditions indicate that auditees have not implemented adequate internal control over compliance for federal programs to ensure compliance with applicable laws and regulations.

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

### ***RJ Ricciardi, CPA, Audit Approach***

RJ Ricciardi, CPA, auditors did not develop a plan to audit Federal awards. The audit program, which includes procedures to be performed for the audit, documents the auditors' determination about whether to include or exclude a compliance requirement from the audit scope. However, the audit program does not include the auditors' justification for excluding a specific compliance requirement. The auditors documented only that the requirement was not applicable. Consequently, independent reviewers cannot understand the auditors' judgment to exclude the requirement from the audit scope. For example, reviewers cannot determine whether the requirement has a material effect or does not apply to the major program.

The auditors performed the financial statement audit and the Federal awards audit together because they determined it was easier to perform one audit. The auditors determined and documented materiality for each major program. As the auditors encountered a Federal expenditure during the financial statement audit, they included the related compliance requirement<sup>13</sup> for that expenditure in the overall audit scope. For

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<sup>12</sup>Assertions are explicit or implicit representations by management that are embodied in financial statements elements (assets, liabilities, revenue, and expenses). The assertions are:

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

<sup>13</sup>Appendix A lists the 14 compliance requirements.

example, during the financial statement audit of equipment expenses, the auditors identified an expenditure related to the Federal awards. Therefore, the auditors included the OMB Circular A-133 equipment and real property management compliance requirement in the audit scope. However, OMB Circular A-133 includes compliance requirements that have no corresponding financial statement expenditure. For example, the reporting and period of availability of Federal funds compliance requirements are not part of a financial statement audit. As a result, the audit scope excluded compliance requirements that are applicable to the major programs.

### *Effect on the Audit*

Because the audit was improperly planned, the auditors did not perform internal control testing for the period of availability of Federal funds compliance requirement (Finding B); and did not adequately document their working papers for work performed, judgments used, and conclusions reached (Finding C). Therefore, the audit was incomplete, and Federal agencies and other report users cannot rely on it.

## **Recommendation, Management's Response, and Evaluation of Response**

**1. We recommend that for the fiscal year 1999 and future years' audits, RJ Ricciardi, CPA, document an audit plan for major programs in accordance with the OMB Circular A-133 requirements. The plan should include documentation to support the auditors' conclusion that, for each of the 14 compliance requirements, the compliance requirement does or does not directly and materially affect the major program.**

**Management's Response.** Concur. The audit firm emphasized that the audit was planned and executed as an organization-wide audit, which included the financial statements and Federal awards. However, the firm agreed that in some cases, the working paper documentation is difficult to follow and that the documentation in the planning and field work areas did not reflect the recent changes to the compliance supplement. The auditors planned the current year's audit using standard working papers purchased from Practioners Publishing Company (PPC), a company that sells standard audit working papers, including those for OMB Circular A-133 audits. The auditors used the PPC working papers for non-profit planning and engagement acceptance and for developing compliance tests for Federal programs. In response to this recommendation, the auditors prepared the PPC planning document for Federal awards. In addition, the auditors had documented the working papers to indicate which of the 14 compliance requirements had a direct and material effect on the major program.

For future years' audits, the auditors agreed to document the audit work performed in compliance with the compliance supplement. The complete text of the audit firm's response is in Appendix F.

**Evaluation of Management's Response.** The completed corrective actions are responsive to the recommendation and are sufficient to close it for reporting purposes.



## **Finding B. Audit of the Period of Availability of Federal Funds and Reporting Requirements**

The RJ Ricciardi, CPA, auditors did not audit the period of availability of Federal funds and reporting compliance requirements for the Institute. This occurred because the auditors did not plan the audit to identify the compliance requirements that have a direct and material effect on the major program. As a result, the audit is incomplete because the auditors did not determine that these requirements are material to the major program. Therefore, Federal agencies and other report users cannot rely on the audit report.

### ***Audit Requirements***

Finding A describes the OMB Circular A-133 and AICPA requirements to plan internal control and compliance testing.

**Audit Objectives.** The OMB Circular A-133 Compliance Supplement states that for the period of availability of Federal funds compliance requirement, the auditors must determine whether Federal funds were used in the time period specified in the award. For the fiscal year 1999 audit, the auditors stated that the period of availability of Federal funds compliance requirement is not applicable to the major program. Compliance Supplement, part 3, section I, "Period of Availability of Federal Funds," describes this requirement as follows:

Federal awards may specify a time period during which the non-Federal entity may use the Federal funds. Where a funding period is specified, a non-Federal entity may charge to the award only costs resulting from obligations incurred during the funding period and any pre-award costs authorized by the Federal awarding agency. Also, if authorized by the Federal program, unobligated balances may be carried over and charged for obligations of the subsequent funding period. Obligations means the amounts of orders placed, contracts and subgrants awarded, goods and services received, and similar transactions during a given period that will require payment by the non-Federal entity during the same or a future period ....

The OMB Circular A-133 Compliance Supplement states that for the reporting compliance requirement, the control objective is:

To provide reasonable assurance that reports of Federal awards submitted to the Federal awarding agency or pass-through entity include all activity of the reporting period, are supported by underlying accounting or performance records, and are fairly presented in accordance with program requirements.

In addition, the compliance audit objective for the reporting requirement is to:

Determine whether required reports for Federal awards include all activity of the reporting period, are supported by applicable accounting or performance records, and are fairly presented in accordance with program requirements.

**Internal Control Documentation Guidelines.** OMB Circular A-133 Compliance Supplement, Part 6, "Internal Control," describes characteristics of internal control for

each of the five components of internal control that should reasonably assure compliance with Federal laws, regulations, and program compliance requirements. Part 6 of the Supplement also provides brief descriptions of the components of internal control and examples of characteristics common to the 14 types of compliance requirements.<sup>14</sup>

Part 6 is intended to assist non-Federal entities and their auditors in complying with the requirements by describing, for each of the 14 compliance requirements, the objectives of internal control and certain characteristics of internal control that, when present and operating effectively, may ensure compliance with program requirements. However, the characteristics reflected in Part 6 may not reflect how an entity considers and implements internal control. Non-Federal entities could have adequate internal control even though some or all of the characteristics in Part 6 are not present. Further, non-Federal entities could have other appropriate internal controls that are operating effectively but are not included in Part 6. Non-Federal entities and their auditors need to exercise judgment in determining the most appropriate and cost-effective internal control in a given environment or circumstance to provide reasonable assurance for compliance with Federal program requirements.

**Requirements to Test Internal Controls.** As stated in Finding A, the auditors must plan the testing of internal control over major programs to support a low assessed level of control risk for the assertions relevant to the compliance requirements for each major program and unless internal control is likely to be ineffective, perform testing of internal control as planned.

**Performing Compliance Tests.** OMB Circular A-133 § \_\_\_.500(d)(1) and (4) and AICPA SOP 98-3, section 6.20, require the auditors to determine whether the Federal award recipient complied with the laws, regulations, and contract and grant provisions that materially affect the major program. Compliance testing includes transactions and other auditing procedures that provide the auditors with sufficient evidence to support an opinion on compliance. Part 3 of the OMB A-133 Compliance Supplement provides the auditors guidance on reviewing compliance with each of the 14 compliance requirements. This information is intended to assist the auditors in planning and performing tests to determine whether the auditee complied with the Federal program requirements. AICPA SOP 98-3, sections 6.39, 6.36, and 6.37, state that the purpose of the compliance testing is for the auditors to apply procedures to provide reasonable assurance of detecting material noncompliance to determine whether the auditee materially complied with the requirements.

### ***RJ Ricciardi, CPA, Audit Approach***

**Planning the Audit.** As explained in Finding A, the auditors did not adequately plan the audit of Federal awards. The audit program is the only document that allows the reviewer to understand which of the 14 compliance requirements were audited. For those

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<sup>14</sup>Appendix A lists the 14 compliance requirements.

requirements identified as not applicable and not audited, the auditors did not document the working papers to support that the requirement did not have a direct and material effect on the major program.

**Period of Availability of Federal Funds Compliance Requirement.** The auditors did not audit the period of availability of Federal funds compliance requirement. The auditors also did not document their working papers to support their conclusion that this requirement was not applicable to the major program. Although the auditors documented in their audit program that this requirement was not applicable, they explained that this requirement is material to the research and development major program and was audited as part of the financial statement audit of accounts payable. Mr. Ricciardi, Partner, explained to us that during the auditors' search for unrecorded liabilities, the auditors identified three Federal awards that were completed at September 30, 1999. The auditors also reviewed a list of the October and November 1999 expenditures for expenditures related to the three awards to ensure that the expenditures were charged to the correct accounting period. However, the auditors did not document their working papers to support that they performed these audit procedures, and they did not perform these procedures for awards that were completed before September 30, 1999.

**Reporting Compliance Requirement.** Mr. Ricciardi explained to us that although the auditors documented in their audit program that the reporting requirement is material and applicable to the major program, there is no working paper documentation to support that the auditors audited this requirement. Mr. Ricciardi further explained that only one report was required for this major program and that he reviewed it while auditing the cash management requirement. He also explained that he mathematically verified the expenditures in the report, reconciled the amounts in the report to the SETI accounting records, and noted that the SETI Institute filed the report in a timely manner. The cash management working paper documentation shows that Mr. Ricciardi reviewed information from the financial report in support of the cash management audit. However, the cash management working papers were not documented to support that the auditors also audited the reporting requirement or performed any of the procedures Mr. Ricciardi discussed with us. In addition, the auditors did not document their understanding of internal controls or plan and perform internal control testing for the reporting requirement.

### ***Effect on the Audit***

The auditors did not plan the audit to identify the compliance requirements that have a direct and material effect on the major program. Consequently, the audit was incomplete because the auditors did not audit the period of availability of Federal funds compliance requirement based on a determination that the requirement was not applicable to the major program. In addition, the auditors did not audit the reporting compliance requirement, even though they concluded that the requirement had a direct and material effect on the major program. Without an audit of these compliance requirements, Federal agencies and others cannot rely on the internal control assurances and compliance opinion in the audit report related to Federal awards.

## **Recommendations, Management's Response, and Evaluation of Response**

**2. We recommend that for the current year's audit, RJ Ricciardi, CPA, audit the period of availability of Federal funds and reporting compliance requirements to include documenting the auditors' understanding of internal controls, testing internal controls, and performing compliance tests**

**3. We recommend that for future years' audits, RJ Ricciardi, CPA, audit each compliance requirement that has a direct and material effect on the major program.**

**Management's Response.** Partially concur with recommendation 2 and concur with recommendation 3. RJ Ricciardi, CPA, stated that its auditors extensively audited the period of availability of Federal funds compliance requirement. However, Mr. Ricciardi agreed that the audit program was completed incorrectly and that the documentation was difficult to follow. For the current year's audit, the auditors used the standard PPC working papers to perform additional work and documented their understanding and testing of internal control for the availability of Federal funds compliance requirement. In response to recommendation 3, Mr. Ricciardi agreed to implement corrective action on future years' audits. The complete text of the audit firm's response is in Appendix F.

**Evaluation of Management's Response.** The completed corrective action for recommendation 2 is partially responsive. After completion of our field work, the auditors adequately documented their tests of internal control and compliance and their understanding of internal control for the period of availability of Federal funds requirement.

Mr. Ricciardi did not address the reporting requirement in his response to recommendation 2. At the time we issued our draft report, the auditors submitted for our review copies of working papers that addressed corrective action on the reporting requirement. The revised and additional working papers included corrective action that satisfactorily meet the intent of the recommendation to document the auditors' tests of internal control and compliance for the reporting requirement. However, the auditors still did not adequately document their understanding of internal control for the reporting compliance requirement, and Mr. Ricciardi did not address this requirement in his response to the draft report. In addition, while Mr. Ricciardi stated that the auditors would implement corrective action in future years in response to recommendation 3, Mr. Ricciardi did not address the reporting compliance requirement in the current year's audit. Therefore, we request that Mr. Ricciardi further review his position on this matter and provide additional comments that specifically address the reporting compliance requirement for the current and future years. The auditors should also document their understanding of internal controls for the reporting compliance requirement and submit to our office the working papers that support the completed corrective action. Recommendations 2 and 3 are unresolved pending review and evaluation of additional comments and documentation.

## **Finding C. Working Paper Documentation**

The RJ Ricciardi, CPA, auditors did not document their working papers for their: (1) determination of major programs; (2) assessment that the SETI Institute is a low-risk auditee; and (3) understanding of internal controls for the activities allowed or unallowed compliance requirement. The auditors also did not document the internal controls relied on and tested for the equipment compliance requirement and the compliance testing performed for the cash management compliance requirement. The auditors have been conducting the audits at the Institute for many years and, therefore, did not take the time to document the routine audit procedures performed annually so that someone not familiar with those procedures can also understand the work performed. Without sufficient working paper documentation, there is no evidence that the audit work was performed in accordance with the requirements of OMB Circular A-133, its related Compliance Supplement, GAGAS, and the AICPA auditing standards. Also, independent reviewers cannot understand the auditors' conclusions and judgments regarding the work performed.

### ***Working Paper Documentation Requirement***

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

### ***Determination of Major Programs***

**Identifying and Documenting Major Programs.** OMB Circular A-133 requires auditors to use the risk-based approach described in §\_\_\_.520 to identify and audit Federal awards that have been identified as major programs. In general, the risk-based approach requires the auditors to determine major programs based on dollar thresholds and risk analyses. The Federal expenditures at the Institute are all part of the research and development program. Part 5 of the OMB Circular A-133 Compliance Supplement requires the auditor to group these expenditures into a program cluster.<sup>15</sup> In accordance with OMB Circular A-133 §\_\_\_.520, all the awards that comprise the research and development program cluster are considered together when determining major programs.

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<sup>15</sup> OMB Circular A-133 Compliance Supplement, Part 5, defines a cluster as "... closely related programs that share common compliance requirements." OMB considers research and development awards a cluster.

OMB Circular A-133 §\_\_\_\_.520(g), "Documentation of risk," states that the auditor must document in the working papers the risk analysis process used in determining major programs.

**Auditors' Determination of Major Programs.** OMB Circular A-133 §\_\_\_\_.500 requires the auditors to plan and perform an audit of each major program. The RJ Ricciardi, CPA, auditors stated in the audit report that NASA and the National Science Foundation were the major programs audited. The working papers do not document the auditors' determination of major programs as required by the Circular, although the auditors stated that the working papers were properly documented. The auditors identified two major programs in the audit report, but performed the audit as if there were only one major program. That is, they audited all the major program expenditures together and performed the Federal awards and financial statement audits as one. Using this approach, the auditors determined which compliance requirements affected all the Federal expenditures and did not make that determination by major program as required by the Circular. All of the expenditures in the research and development program cluster should have been audited together as one Federal program. Had the auditors followed the risk-based approach outlined in the Circular, they would have documented their working papers to show that all the awards were research and development and would have correctly identified research and development as the major program in the audit report. As a result of the insufficient working paper documentation, independent reviewers cannot understand why the auditors identified NASA and the National Science Foundation programs as the major programs in the audit report.

#### ***Low-Risk Auditee Documentation***

The auditors did not document their working papers to support the statement in the audit report that the SETI Institute is a low-risk auditee. OMB Circular A-133 §\_\_\_\_.520(f) allows an auditee to be eligible for reduced audit coverage (low-risk auditee) if it meets all the stated conditions in OMB Circular A-133 §\_\_\_\_.530 for each of its preceding 2 fiscal years. The auditors are required to audit 25 percent of the Federal expenditures for low-risk auditees, compared to auditing 50 percent of expenditures for organizations that are not classified as low-risk auditees. The auditors determined that the SETI Institute met the conditions to be classified as a low-risk auditee but did not document their working papers to support that conclusion and included all the Institute's Federal expenditures in their audit scope. Therefore, the auditors did not reduce the audit coverage. Consequently, report readers may rely on the low-risk auditee determination to gain information about past reports without reading those reports. For example, one of the criterion for low-risk status is that the auditee received an unqualified opinion on its financial statements in the last 2 years. For the 1999 SETI Institute audit, this should mean that the Institute received unqualified opinions for its 1998 and 1997 fiscal years. All of the criteria must be met every year for the auditee to be classified as low-risk. However, for the 1999 audit, there is no working paper support to show that the SETI Institute met the criteria. Therefore, the low-risk determination is unreliable.

### *Understanding and Testing Internal Controls*

The auditors did not document their working papers for their understanding of internal controls for the activities allowed or unallowed compliance requirement. The auditors also did not document their working papers for the internal controls relied on and tested for the equipment management compliance requirement.

**Internal Control Requirements.** In addition to the internal control characteristics, OMB Circular A-133 Compliance Supplement, Part 6, identifies the control objectives for each compliance requirement. For the activities allowed or unallowed compliance requirement, the control objective is:

To provide reasonable assurance that Federal awards are expended only for allowable activities and that the costs of goods and services charged to Federal awards are allowable and in accordance with the applicable cost principles.

The internal control objective for the equipment management compliance requirement is:

To provide reasonable assurance that proper records are maintained for equipment acquired with Federal awards, equipment is adequately safeguarded and maintained, disposition or encumbrance of any equipment or real property is in accordance with Federal requirements, and the Federal awarding agency is appropriately compensated for its share of any property sold or converted to non-Federal use.

As previously discussed, OMB Circular A-133 requires the auditors to document their understanding of internal controls, and Part 6 of the OMB Circular A-133 Compliance Supplement describes characteristics of internal control for each compliance requirement. As also previously discussed, OMB Circular A-133 requires the auditors to plan the testing of internal control over major programs and unless internal control is likely to be ineffective, requires auditors to perform testing of internal control as planned.

**Documentation and Audit of Internal Controls.** As described in Finding A, the auditors did not plan the audit to meet OMB Circular A-133 audit requirements. The audit approach did not include a plan to identify and audit the compliance requirements that have a direct and material effect on the major program. Instead, the auditors audited the compliance requirements as they encountered a Federal expenditure. This approach did not enable the auditors to cover all of the audit requirements, such as documenting and testing internal controls.

For the activities allowed or unallowed compliance requirement, the auditors tested Federal and non-Federal, payroll and nonpayroll expenditures together. The auditors also tested internal controls related to these expenditures. However, the auditors did not document their working papers for their understanding of internal controls for this compliance requirement as required by OMB Circular A-133.

The auditors did not document the internal controls relied on and tested for the equipment and procurement and suspension and debarment compliance requirements. The auditors identified one equipment expenditure of about \$10,000, purchased with Federal awards in

1999. Through the financial statement audit, the auditors documented the equipment internal control policies and procedures instituted by the Institute and audited the expenditure. However, the auditors did not document their internal control testing for the equipment compliance requirement.

Without sufficient documentation of the auditors' understanding and testing of internal controls, there is no basis for report users to rely on the audit report's assurance that internal controls are in place and operating effectively.

### ***Testing Compliance***

The auditors did not document their working papers for the compliance testing performed for the cash management requirement. Findings A and B describe the OMB Circular A-133 and AICPA requirements to plan and perform the compliance testing for each requirement. OMB Circular A-133 Compliance Supplement, Part 3, "Compliance Requirements," identifies the audit objectives for each compliance requirement. For the cash management compliance requirement, the auditors must determine whether (1) the entity paid for the program costs before requesting reimbursement from the Federal Government when entities are funded on a reimbursement basis or whether (2) the entity minimized the elapsed time between the transfer of funds from the U.S. Treasury and disbursement if the entity received an advance payment. The audit working papers that support an audit of the cash management requirement include those created by the auditors and requested from the SETI Institute by the auditor. Without extensive oral explanations, independent reviewers cannot determine the purpose of the supporting working papers or how they satisfy the audit objectives and the procedures detailed in the summary working paper. The supporting working papers show numbers but provide no explanation about their purpose. As a result of insufficient documentation of the auditors' compliance testing and conclusions, there is no basis for report users to rely on the audit report opinion that the Institute materially complied with the laws, regulations, and agreement provisions for fiscal year 1999.

### ***Effect on the Audit***

Sufficient working paper documentation permits independent reviewers to determine whether the audit was adequately planned and executed to meet the OMB Circular A-133 audit objectives. The documentation also provides a basis for the independent reviewer to determine whether Federal agencies and other users can rely on the internal control assurances and the opinions in the audit report. Without sufficient working paper documentation, (1) there is no evidence that the audit work was performed in accordance with the requirements of OMB Circular A-133, its related Compliance Supplement, GAGAS, and the AICPA auditing standards and (2) independent reviewers cannot understand the auditors' conclusions and judgments regarding the work performed. In addition, audit report users have no basis to rely on the auditors':

- determination of major programs;
- low-risk auditee classification;



- understanding of internal controls for the activities allowed or unallowed compliance requirement;
- identification of the internal controls relied on and tested for the equipment and procurement and suspension and debarment compliance requirements; and
- details for the compliance tests performed for the cash management compliance requirement.

## **Recommendations, Management’s Response, and Evaluation of Response**

**We recommend that in the current and future years’ audits, RJ Ricciardi, CPA, require auditors to document their working papers to:**

- 4. Support their determination of major programs as required by OMB Circular A-133.**
- 5. Support their assessment of the low-risk auditee classification for the SETI Institute.**
- 6. Explain their understanding of internal controls for the activities allowed or unallowed compliance requirement.**
- 7. Identify the internal controls relied on and tested for the equipment compliance requirement.**
- 8. Identify the compliance testing performed for the cash management compliance requirement.**

**Management’s Response.** Concur. Management completed corrective action in the current year and agreed to implement the corrective action in future years’ audits for recommendations 4 through 6. In response to recommendation 7, the auditors revised their working papers to identify the internal controls relied on and tested for the equipment compliance requirement and referenced the working papers that contain the auditors’ tests of the internal controls. For recommendation 8, the auditors included additional explanations and references in the summary working paper to identify the compliance tests documented in the supporting working papers for the cash management requirement. The complete text of the response is in Appendix F.

**Evaluation of Management’s Response.** For recommendations 4 through 6, the completed corrective action in the current year and the planned corrective action for future years’ audits are responsive to the recommendations and are sufficient to close the recommendations for reporting purposes.

Mr. Ricciardi’s comments are not fully responsive to recommendations 7 and 8. Although the completed corrective action for the current year’s audit is responsive, Mr. Ricciardi did not address the planned corrective action for future years’ audits.

Therefore, we request that Mr. Ricciardi further review his position on this matter and provide additional comments that specifically address corrective action in future years to identify the (1) internal controls relied on and tested for the equipment compliance requirement and (2) compliance testing performed for the cash management requirement. Recommendations 7 and 8 are unresolved pending review and evaluation of the additional comments.

## **Appendix A. Single Audit Requirements**

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

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

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

The revised OMB Circular A-133 was issued 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 independent standards in generally accepted government auditing standards and in accordance with the auditing and reporting requirements of the Circular and its related Compliance Supplement. The audit report submission contains:

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

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

The Compliance Supplement is based on the requirements of the Single Audit Act Amendments of 1996 and the final June 30, 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 also identifies existing and important compliance requirements, which the Federal Government expects the auditors to consider as part of an audit required by the 1996 Amendments. Using the Supplement eliminates the need for the auditors to research the laws and regulations for each major program audit to determine the compliance requirements that are important to the Federal Government and that could have a direct and material effect on the major program. The Supplement is a more efficient and cost-effective approach to performing this research. It "... provides a source of information for auditors to understand the Federal program's objectives, procedures, and compliance requirements relevant to the audit as well as audit objectives and suggested audit procedures for determining compliance with the requirements."

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

1. Activities Allowed or Unallowed
2. Allowable Costs/Cost Principles
3. Cash Management
4. Davis-Bacon Act
5. Eligibility
6. Equipment and Real Property Management
7. Matching, Level of Effort, Earmarking
8. Period of Availability of Federal Funds
9. Procurement and Suspension and Debarment
10. Program Income
11. Real Property Acquisition/Relocation Assistance
12. Reporting
13. Subrecipient Monitoring
14. Special Tests and Provisions

## **Appendix A**

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

## **Appendix B. Objectives and Scope**

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### **Audit Report Review**

Our objective for the audit report review was to determine whether the report submitted by the auditee meets the applicable reporting standards and the OMB Circular A-133 reporting requirements. As the oversight Federal audit agency for the SETI Institute, we performed a review of the audit report on the SETI Institute for the fiscal year ended September 30, 1999. 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 reports' qualitative aspects of: (1) due professional care; (2) auditor's qualifications and independence; (3) financial statements, compliance, and internal control reporting; (4) Schedule of Expenditures of Federal Awards; and (5) Schedule of Findings and Questioned Costs.

### **Quality Control Review**

Our objectives for the quality control review were to ensure that the audit was conducted in accordance with generally accepted government auditing standards<sup>16</sup> and generally accepted auditing standards and whether the audit meets the auditing and reporting requirements of OMB Circular A-133. As the oversight audit agency for the SETI Institute, we conducted a quality control review of the RJ Ricciardi, CPA, audit working papers. We focused the review on the qualitative aspects of the audit, which include:

- auditor's 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 organized our review by the general and field work audit standards and the required elements of a single audit. We emphasized the areas of major concern to the Federal Government such as determining and auditing major program compliance and internal

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<sup>16</sup>These standards are broad statements of the auditors' responsibilities, promulgated by the Comptroller General of the United States.

## **Appendix B**

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controls. We conducted the review April 16 through 18, 2001, at the San Rafael, California, office of RJ Ricciardi, CPA. We also visited the Mountain View, California, office of the SETI Institute on April 19, 2001. The NASA Office of Inspector General has not previously performed quality control reviews of the RJ Ricciardi, CPA, working papers.

### **Peer Review Report**

We reviewed the January 6, 1998, report on the most recent peer review of RJ Ricciardi, CPA, performed by Vavrinek, Trine, Day & Co., LLP. The Vavrinek, Trine, Day & Co., LLP review determined that RJ Ricciardi, CPA, met the objectives of the quality control review standards established by the American Institute of Certified Public Accountants and that RJ Ricciardi, CPA, complied with the standards during the fiscal year ended May 31, 1997.

## **Appendix C. Quality Control Review Methodology**

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### **Independent Auditor's Report**

The auditors are required to determine whether the financial statements are presented fairly in all material respects in conformity with generally accepted auditing principles and are free of material misstatement. The auditors are also required to subject the Schedule of Expenditures of Federal Awards to the procedures applicable to the audit of the financial statements and to ensure that the amounts are fairly stated in relation to the basic financial statements. We reviewed the RJ Ricciardi, CPA (Certified Public Accountant), audit programs and the testing of evidence to determine whether testing was sufficient based on an assessment of control risk to warrant the conclusion reached. We also reviewed the working papers to determine whether they supported the conclusion.

### **Schedule of Expenditures of Federal Awards**

The recipient is responsible for creating the Schedule of Federal Awards. The auditors are required to audit the information in the Schedule to ensure it is fairly presented in all material respects in relation to the financial statements taken as a whole. We reviewed the RJ Ricciardi, CPA, audit programs for the appropriate procedures and traced some of the amounts from the Subsidiary Ledger and/or Trial Balance to the Schedule.

### **Independent Auditor's Report on Compliance and on Internal Control over Financial Reporting Based on an Audit of Financial Statements Performed in Accordance with Government Auditing Standards**

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

### **Independent Auditor's Report on Compliance with Requirements Applicable to Each Major Program and Internal Controls over Compliance in Accordance with OMB [Office of Management and Budget] 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. 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.



## **Appendix C**

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We also reviewed the working paper documentation and its support and the compliance tests performed. Finally, we retested selected compliance transactions that RJ Ricciardi, CPA, originally tested.

The auditors must perform procedures to obtain an understanding of internal controls over Federal programs that is sufficient to plan an audit to support a low-assessed level of control risk for major programs. The auditors must plan and perform internal controls testing over major programs to support a low level of control risk for the assertions relevant to the compliance requirements for each major program. We reviewed the audit programs for the appropriate procedures, the working paper documentation, and the control tests performed.

### **Findings, Questioned Costs and Recommendations**

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

## **Appendix D. Quality Control Review Referral**

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The President's Council on Integrity and Efficiency (PCIE) Position Statement 4, "IG [Inspector General] Quality Control Referral Procedures," describes the uniform Inspector General policies and procedures for making referrals and the uniform Inspector General referral package. According to the PCIE:

A referable action is when the audit report or underlying audit work have significant inadequacies which make the audit so pervasively deficient that users can not rely on it. The following are significant inadequacies.

1. The auditor is unqualified, i.e., not properly licensed as a CPA [Certified Public Accountant] or public accountant or not independent.
2. Working papers are sufficiently inadequate to preclude an assessment of the adequacy of the auditor's work on the study of internal controls or the testing of compliance requirements; the deficiency is pervasive rather than isolated.
3. A major component of the report is missing, e.g., financial statement(s), opinion, report on compliance, required supplemental schedule, etc.
4. The auditor fails to correct substandard work on a timely basis.
5. The auditor fails to review compliance with requirements.
6. The auditor fails to perform an appropriate evaluation of internal controls.
7. The auditor commits one or more other gross departures from GAGAS [generally accepted government auditing standards] which undermines the credibility of the audit. Some examples are:
  - lack of due professional care;
  - lack of sufficient evidential matter;
  - unjustified use of audit guide(s) not considered generally accepted; and
  - lack of site visits

Based on the results of our quality control review, we determined that RJ Ricciardi, CPA, audit work meets the PCIE definition of a referable action under its Position Statement 4. The underlying audit work has significant inadequacies that make the audit unreliable. The working papers are sufficiently inadequate to preclude an assessment of the adequacy of the auditors' work on the study of internal controls and the testing of compliance requirements. In addition, the auditors did not perform an appropriate evaluation of internal controls. Overall, the auditors did not exercise due professional care in planning and performing the audit. Therefore, we will refer the staff assigned to the SETI Institute audit to the American Institute of Certified Public Accountants.

## Appendix E. Other Matters of Interest

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During the quality control review at the Search for Extraterrestrial Intelligence (SETI) Institute, we identified issues related to reporting that should be brought to management's attention but do not affect the results of our review. The issues are described below:

**Schedule of Expenditures of Federal Awards Presentation.** The SETI Institute did not prepare the Schedule of Expenditures of Federal Awards in accordance with Office of Management and Budget (OMB) Circular A-133. In addition, the Institute did not prepare the notes to the schedule as required by the Circular.

OMB Circular A-133 §\_\_\_\_.310(b) requires the auditee to prepare a Schedule of Expenditures of Federal Awards that identifies individual Federal programs and the related program expenditures for the auditee's year end. In addition to awards received directly from the Federal government, the auditee also includes in the Schedule awards received from pass-through entities<sup>17</sup> and awards provided to subrecipients.<sup>18</sup> Section \_\_\_\_310(b)(1) states that, at a minimum, the Schedule will identify the individual Federal programs by Federal agency. For Federal programs that are included in a cluster of programs,<sup>19</sup> the auditee will list the individual Federal programs within the cluster. For the research and development cluster, the auditee will identify the total Federal awards expended either by the individual award or by Federal agency and major subdivision within the Federal agency.

OMB Circular A-133 §\_\_\_\_.310(b)(4) requires the auditee to prepare notes to the Schedule of Expenditures of Federal Awards. The purpose of the notes is to describe the significant accounting policies used in preparing the Schedule. In addition, the auditee must include, in either the Schedule or a note to the Schedule, the value of the Federal awards expended in the form of non-cash assistance, the amount of insurance in effect during the year, and loans or loan guarantees outstanding at year end.

The SETI Institute prepared a Schedule of Expenditures of Federal Awards that did not identify all the awards in the Schedule as part of the research and development program cluster. The auditee identified the NASA and the National Science Foundation (NSF) awards, along with the award the Institute (subrecipient) received from the Universities Space Research Association (pass-through entity). Through discussions with the auditors and SETI management and a review of award documents, we determined that all of the awards in the Schedule are for research and development. However, the Institute

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<sup>17</sup>OMB Circular A-133 §\_\_\_\_.105, "Definitions," states that a pass-through entity is "... a non-Federal entity that provides a Federal award to a subrecipient to carry out a Federal program."

<sup>18</sup> OMB Circular A-133 §\_\_\_\_.105, "Definitions," defines a subrecipient as "... a non-Federal entity that expends Federal awards received from a pass-through entity to carry out a Federal program .... A subrecipient may also be a recipient of other Federal awards directly from a Federal awarding agency."

<sup>19</sup>See footnote 14.

did not identify these awards as research and development in the Schedule or in the notes that are required by the Circular because the Institute's management did not know the requirements for the presentation of the Schedule or the notes.

Because the Schedule does not identify the types of awards, the audit report users do not know the types of awards the Institute received from the Federal Government. Also, Federal agencies do not know which accounting policies the Institute used to prepare the Schedule. Disclosing this information in the audit report assists the report user in determining the appropriate procedures to administer Federal awards.

**Management's Response.** Concur. SETI Institute management agreed that for future years' audits, the Institute would prepare the Schedule of Expenditures of Federal Awards in accordance with OMB Circular A-133 and include the required explanatory notes. The complete text of the response is in Appendix G

**Evaluation of Management's Response.** Management's planned corrective action for future years' audits is responsive.

## Appendix F. RJ Ricciardi, CPA, Response

**R. J. RICCIARDI**

CERTIFIED PUBLIC ACCOUNTANT

1000 FOURTH STREET • COURTHOUSE SQUARE • SAN RAFAEL, CALIFORNIA 94901 • (415) 457-1215

October 15, 2001

Ms. Vera J. Garrant, CPA  
A-133 Audit Manager  
NASA-OIG  
Headquarters, Code W  
300 E Street SW  
Washington, DC 20546

Re: Response to your draft report

Dear Vera:

Thank you for sending us the draft report. I appreciate your assistance during various phone conversations.

The attached responses should answer all your concerns. In some instances, we were unsure of the scope of your finding, but feel we have addressed it. If by chance we missed something, please give us an opportunity to respond. If a second or revised draft would be beneficial we would appreciate the opportunity to review and respond to it.

Very truly yours,

*Ralph J. Ricciardi/CPA*

Ralph J. Ricciardi  
Certified Public Accountant

RJR:es

**Recommendation For Corrective Action #1 & 3**

Our audit plan for Major Programs consisted of procedures documented in the planning section of the PPC Audits of Federal Awards Programs - General Procedures. We also followed the PPC Non-Profit Organization Audit Planning Form and Engagement Acceptance and Continuation Form. Another PPC document used was the Audits of Federal Awards Programs - Developing Tests of Compliance for Programs not included in the Compliance Supplement. Most of these procedures were performed in the planning stages of the audit. As a corrective action I have prepared for the current year, and will prepare for future years, the attached PPC Planning Form - Audits of Federal Awards Programs. As an additional corrective action, I have prepared a working paper to document the auditors conclusion that which of the 14 compliance requirements does or does not directly and materially affect the major program. The working papers noted above have been attached for your review. Although a financial audit is part of the Single Audit, R.J. Ricciardi has only performed single audits for the organization (We have not issued a separate financial statement audit.) The cover of the report is titled Single Audit. The entire planning and audit process is geared toward the OMB and grant regulations. The non-federal transactions are in most cases reviewed for compliance with these regulations, even though this is not required. We concur in some instances, the documentation is hard to follow and our documentation for procedures performed in the planning and fieldwork stages did not reflect the recent changes to the compliance supplement. We are confident that the audit work performed, accomplished the audit objectives in the compliance supplement. Our documentation of the audit work performed will be in compliance with the compliance supplement in future audits.

**Recommendation for Corrective Action #2**

We do not concur completely with this finding. We extensively audited for the compliance requirement Period Availability of Federal Funds. We do concur that the Federal Awards Audit Program was not completed correctly and the documentation was hard to follow. As a corrective action, the Federal Awards Audit Program has been noted in red. I have also completed the documentation for Control Environment, Activities, Risk, Information and Monitoring. Our corrective actions will be implemented in future audits.

**Recommendation for Corrective Action #4 & 5**

The corrective action has been forwarded to Ms. Garrant and will also be implemented for future audits.

**Recommendation for Corrective Action #6**

The corrective action has been forwarded to Ms. Garrant and will also be implemented for future audits.

**Recommendation for Corrective Action #7**

The equipment and real property compliance documentation for Control Environment, Activities, Risk, Information and Monitoring is attached. The federal and non-federal equipment purchases have the same internal control system. The internal controls were tested in sections, 7100, 2500, 3000 and 3100. As a corrective action, we have noted procedures documented on the Federal Awards Audit Program also on the individual working papers.

**Recommendation for Corrective Action #8**

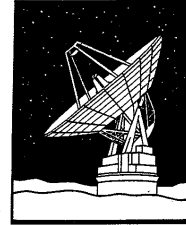
The compliance testing performed for cash management is stated on the attached working paper 7300. Per your E-mail dated October 5, 2001 we have the attached working papers with additional notes and references to the procedures summary page. Also in working paper 4000, cash draw down supporting working papers were reviewed when reviewing revenue detail. We are not sure what else you need for cash management and reporting? We feel we tested this thoroughly.

R. J. RICCIARDI

## Appendix G. Search for Extraterrestrial Intelligence Response

September 24, 2001

Mr. Alan J. Lamoreaux  
National Aeronautics and Space Administration  
Headquarters  
Washington, DC 20546-0001



SETI Institute  
2035 Landings Drive  
Mtn. View, CA 94043  
(650) 961-6633  
Facsimile (650) 961-7099  
www.seti.org

Re: Response to draft report on Quality Control Review of RJ Ricciardi, CPA audit of Search for Extraterrestrial Intelligence Institute for the fiscal year ended September 30, 1999, Assignment no. A-01-025-00.

Dear Mr. Lamoreaux:

I have reviewed the quality control review report of RJ Ricciardi, CPA's audit of the SETI Institute for the fiscal year ended September 30, 1999. I am responding only to Appendix E of this report titled "Other Matters of Interest" in which reporting issues were brought to the attention of the SETI Institute's management. During the review of the audit it was determined that the Institute's management did not prepare the Schedule of Expenditures of Federal Awards Presentation in complete accordance with the OMB Circular A-133.

The SETI Institute's management concurs with this notation and agrees to complete future schedules in accordance with OMB Circular A-133 and will include the required explanatory notes. In order to ensure that these changes take place Institute management has done a thorough review of the requirements stated in the OMB Circular A-133 and has made extensive notes to the file outlining how the future Schedules of Expenditures of Federal Awards should be prepared. These notes will be consulted when the future Schedules of Expenditures of Federal Awards are prepared and all requirements will be included.

Thank you for your help with this matter. If you have any questions or need any additional information, please contact me at (650) 960-4520.

Sincerely,

A handwritten signature in cursive script that reads "Shannon L. Atkinson".

Shannon L. Atkinson, CPA  
Chief Financial Officer

## **Appendix H. Report Distribution**

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### **Audit Firm/Auditor**

Mr. Ralph J. Ricciardi  
1000 Fourth Street, Suite 725  
San Rafael, CA 94901

### **Audited Organization**

Ms. Shannon Atkinson  
Chief Financial Officer  
SETI Institute  
2035 Landings Drive  
Mountain View, CA 94043-0818

### **Administrative Contracting Officer**

Mrs. Debbie Rafi, Director  
Indirect Cost Division  
Office of Naval Research  
University Business Affairs  
Ballston Tower #1, Room 704  
800 North Quincy Street  
Arlington, VA 22217-5660

### **Federal Office of Inspector General**

National Science Foundation

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

A/Acting Administrator  
AB/Associate Deputy Administrator for Institutions  
AA/Chief of Staff  
AO/Chief Information Officer  
B/Acting Chief Financial Officer  
B/Comptroller  
BF/Director, Financial Management Division  
G/General Counsel  
H/Associate Administrator for Procurement  
JM/Director, Management Assessment Division



**NASA Field Installation**

Director, Ames Research Center  
Director, Goddard Space Flight Center  
Acting Director, Lyndon B. Johnson Space Center

**Executive Office of the President**

Office of Management and Budget, Office of Federal Financial Management

## NASA Assistant Inspector General for Auditing Reader Survey

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

**Report Title:** Quality Control Review of RJ Ricciardi, CPA, Audit of the Search for Extraterrestrial Intelligence (SETI) Institute for Fiscal Year Ended September 30, 1999 (Assignment No. A-01-025-00)

**Report Number:** \_\_\_\_\_ **Report Date:** \_\_\_\_\_

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     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.**

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***How did you use the report?***

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***How could we improve our report?***

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***How would you identify yourself? (Select one)***

- |   |  |
|---|--|
| <input type="checkbox"/> Congressional Staff  | <input type="checkbox"/> Media           |
| <input type="checkbox"/> NASA Employee  | <input type="checkbox"/> Public Interest |
| <input type="checkbox"/> Private Citizen  | <input type="checkbox"/> Other: _____    |
| <input type="checkbox"/> Government: _____ Federal: _____ State: _____ Local: _____ |  |

***May we contact you about your comments?***

\_\_\_\_ Yes.  
Name \_\_\_\_\_  
Telephone Number: \_\_\_\_\_

\_\_\_\_ No.

Thank you for your cooperation in completing this survey.

## **Major Contributors to the Report**

Patrick A. Iler, Director, Audit Quality

Vera J. Garrant, A-133 Audit Manager

Nancy C. Cipolla, Report Process Manager

Karen Vance, Program Assistant