Oversight Report

QUALITY CONTROL REVIEW OF JOHN T. PIERCE, D.P.A.,P.A.
AND THE DEFENSE CONTRACT AUDIT AGENCY
NORTHEAST CONSORTIUM FOR
ENGINEERING EDUCATION, INC.
FISCAL YEAR ENDED DECEMBER 24, 1996

Report Number PO 98-6-014 July 27, 1998

Office of the Inspector General
Department of Defense

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Acronyms

DCAA	Defense Contract Audit Agency
GAAS	Generally Accepted Auditing Standards
GAO	General Accounting Office
GAS	Government Auditing Standards
NCEE	Northeast Consortium for Engineering Education, Inc.
JTP	John T. Pierce, C.P.A, P.A.
OMB	Office of Management and Budget

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July 27, 1998

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SUBJECT: Quality Control Review of John T. Pierce, C.P.A., P.A.
and the Defense Contract Audit Agency
Northeast Consortium for Engineering Education, Inc.
Fiscal Year Ended December 31, 1996
Report No. PO98-6-014 (Project No. 8OA-9-008.07)

Introduction

We are providing this report for your information. The firm of John T. Pierce, C.P.A, P.A. (JTP) and the Defense Contract Audit Agency (DCAA), performed the single audit for the Northeast Consortium for Engineering Education, Inc. (NCEE), Port Royal, Virginia, a nonprofit organization. The audit is required by Office of Management and Budget (OMB) Circular A-133, "Audits of Institutions of Higher Education and Other Nonprofit Institutions." For the fiscal year ended December 31, 1996, the NCEE reported total Department of Defense (DoD) Federal expenditures of $3,723,202.

The JTP audit report, dated June 28, 1997, includes individual reports on internal controls, compliance, and the Schedule of Federal Awards. JTP issued a unqualified opinion on the financial statements, Schedule of Federal awards, and compliance with specific requirements applicable to the major programs. The DCAA issued its incurred costs audit report on January 28, 1998. The DCAA questioned $68,000 related to program operations and management indirect costs claimed on Federal cost reimbursable awards. Questioned costs result primarily from reallocation of indirect labor cost.

JTP issued positive and negative assurance statements on compliance with general requirements. Positive assurance means that, with respect to the items tested, the results of auditors' procedures disclosed no material instances of noncompliance. Negative assurance means that, with respect to the items not tested, nothing came to the auditors' attention that caused them to believe that NCEE has not complied in all material respects.

JTP obtained an understanding of the internal controls related to the financial statements and Federal awards. The audit report describes the auditors' scope of work in obtaining that understanding and in assessing control risk. The report on internal controls further describes the significant internal controls, including reportable conditions, material weaknesses, and controls that provide reasonable assurance that Federal awards are being managed in accordance with applicable laws and regulations.

Quality Control Review Results

The OMB Circular A-133 audit performed by JTP meets the applicable guidance and regulatory requirements in OMB Circular A-133 and its related Compliance Supplement, which incorporate the Government Auditing Standards (GAS) and Generally Accepted Auditing Standards (GAAS). The DCAA part of the audit generally meets the standards; however, we found that the DCAA documentation of its sampling plan, which supports the transaction testing for Federal program compliance, was not sufficiently documented and did not fully comply with GAS, paragraph 4.34, 4.35, and 4.37a. The GAS requirement specifies that the auditors' work be retained in the form of working papers and that the working papers contain sufficient information to enable an experienced auditor having no previous connection with the audit to ascertain the evidence that supports the auditors' significant conclusions and judgments. Furthermore, the working papers must contain objectives, scope and methodology, and any sampling criteria used. We were able to determine with auditor assistance that the auditors' performed sufficient transaction testing; therefore, we are not requiring additional transaction testing for the subject audit. However, DCAA should ensure that its working papers on future OMB Circular A-133 audits comply with the above GAS requirements.

Quality Control Review Objective

The objective of a quality control review is to ensure that the audit was conducted in accordance with applicable standards and meets the auditing requirements of OMB Circular A-133. As the Federal oversight agency for the NCEE, we conducted a quality control review of JTP and DCAA audit working papers for their audit of the NCEE. We focused our review on the following qualitative aspects of the audit: due

professional care, planning, supervision, independence, quality control, internal controls, substantive testing, general and specific compliance testing, and the Schedule of Federal Awards.

We reviewed the most recent peer review letter dated October 9, 1997, prepared by Robert W. Sim, CPA, on JTP. The peer review found that JTP met the objectives of the quality control review standards established by the American Institute of Certified Public Accountants and that the standards were being complied with during the fiscal year ended June 30, 1997.

Scope and Methodology

We used the 1991 edition of the Uniform Quality Control Guide for Single Audits (the Guide) that was approved by the President's Council on Integrity and Efficiency as guidance for performing the quality control review procedures. The Guide is organized by the general and field work audit standards and the required elements of a single audit. The Guide is further divided into the substantive work performed during the audit of the financial statements and the specific program compliance testing for major programs. In addition, we supplemented the Guide to include additional review of transaction testing.

We conducted our review from April 27 through May 1, 1998. Our quality control review of the audit working papers covered areas related to the financial statements and the awards identified in the Schedule of Federal Awards.

Results of Prior Quality Control Reviews

We have not previously performed a quality control review of JTP.

Background

The Inspector General Act of 1978, Public Law 95-452, prescribes the duties and responsibilities of the Office of Inspector General. In implementing those responsibilities, the Inspector General is required 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) (the Act) was intended to improve the financial management of state and local governments that had total annual expenditures of $100,000 or more with respect to Federal financial assistance programs; to establish uniform requirements for audits of Federal financial assistance; to promote efficient and effective use of audit resources; and to ensure that Federal departments and agencies rely on and use the audit work done under the Act, to the maximum extent practicable.

The OMB Circular A-133 establishes the Federal audit and reporting requirements for nonprofit and educational institutions whose Federal awards are or exceed $100,000. It provides that an audit made in accordance with the Circular shall be in lieu of any financial audit required under individual Federal awards. An agency must rely on the audit to the extent that it provides the information and assurances that an agency needs to perform its overall responsibilities. The coordinated audit approach provides for the independent public accountant, Federal auditor, and other non-Federal auditors to consider each other's work in determining the nature, timing, and extent of their respective audit procedures. The Circular also requires that the cognizant agency obtain or conduct quality control reviews of selected audits made by non-Federal auditors and provide the results, when appropriate, to other interested organizations.

The Single Audit Act Amendments (the Amendments) were signed into law on July 5, 1996. The OMB Circular A-133 was revised and re-titled, "Audit of States, Local Governments, and Non-Profit Organizations." The revised circular establishes uniform audit requirements for non-Federal entities that administer Federal awards, implements the Single Audit Act Amendments of 1996, and consolidates the audit requirements for state and local governments and non-profit organizations under one Circular. The revised Circular applies to audits of fiscal years beginning after June 30, 1996. After 12 years of experience under the 1984 Act, the Amendments are intended to strengthen the usefulness of the single audits by increasing the audit threshold from $100,000 to $300,000 in Federal awards before an audit is required; by selecting programs to be audited on the basis of risk assessment rather than the amount of funds involved; and by improving the contents and timeliness of single audits.

Discussion of Results

During our quality control review, we reviewed and took no exception to the working papers supporting the following reports:

Independent Auditor's Report on Financial Statements. The auditor is required to obtain reasonable assurance about whether the financial statements are free of material misstatement. We reviewed the audit program and the testing of evidence to determine whether testing was sufficient based on assessment of control risk to warrant the conclusion reached and whether the working papers supported the conclusion.

Independent Auditor's Report on Schedule of Federal Awards. The auditor is required to subject the Schedule of Federal Awards to the auditing 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. Our review was included in the steps of evaluation of the audit working papers related to the Independent Auditors' Report.

Schedule of Federal Awards. The recipient is responsible for creating the Schedule of Federal Awards. The auditor is required to audit the information in the Schedule and to ensure that it identifies major programs, as defined by OMB Circular A-133, and total expenditures for each program. We reviewed the audit program for the appropriate procedures, reviewed a selected number of footings/cross footings, and traced some of the amounts to the subsidiary Ledger and/or Trial Balance.

Independent Auditor's Report on Internal Control Structure in Accordance with Government Auditing Standards. The auditor is required to obtain an understanding of the internal control structure that is sufficient to plan the audit and to assess control risk for the assertions embodied in the financial statements. We reviewed the audit program for the appropriate procedures, the working paper documentation, and the substantive testing performed.

Independent Auditor's Report on Internal Control Structure in Accordance with OMB Circular A-133. The auditor is required to obtain an understanding of the internal controls to assess control risk to determine whether the auditor intends to rely on the internal controls. The auditor must perform tests of controls to evaluate the effectiveness of the design and operation of the policies and procedures in preventing or detecting material noncompliance, review the system for monitoring subrecipients and obtaining and acting on subrecipient audit reports, and to determine whether controls are effective to ensure that direct and indirect costs are calculated and billed in accordance with the requirements in the Compliance Supplement. We reviewed the audit program for the appropriate procedures, the working paper documentation, and the test of controls performed.

Independent Auditor's Report on Compliance in Accordance with Government Auditing Standards. The auditor is required to determine whether the recipient has complied with laws and regulations that may have a direct and material effect on the determination of financial statement amounts. We reviewed the audit program for the appropriate procedures, the working paper documentation, its support, and the compliance tests performed.

Independent Auditor's Report on Compliance with General Requirements. The auditor is required to determine whether the recipient has complied with laws and regulations that may have a direct and material effect on any of its major Federal programs. General requirements are those that could have a material effect on the recipient's financial statements including those prepared for Federal programs. The auditors' procedures were limited to those prescribed in the OMB Circular A-133 Compliance Supplement. We reviewed the audit program for the appropriate procedures, compared the audit program steps to those in the Compliance Supplement to make sure that all areas were audited, reviewed the working paper documentation and its support, reviewed the compliance tests performed, and reevaluated selected compliance items.

Independent Auditor's Report on Compliance With Specific Requirements. The auditor is required to determine whether the recipient has complied with laws and regulations that may have a direct and material effect on its major Federal programs, including types of services allowed or unallowed; eligibility; matching, level of effort, and/or earmarking requirements; special reporting requirements; and special tests and provisions. We reviewed the audit program for the appropriate procedures, checked the audit program steps to those in the Compliance Supplement to make sure all areas were audited, reviewed the working paper documentation and its support, reviewed the compliance tests performed, and re-evaluated selected compliance items.

Comments

Because this report contains no recommendations, written comments are not required. We appreciate the courtesies extended during the review. If you have questions on this report, please contact Ms. Barbara Smolenyak, at (703) 604-8760. The report distribution is enclosed.

Donald E. Davis
Deputy Assistant Inspector General
Audit Policy and Oversight

Enclosure

Northeast Consortium for Engineering Education, Inc.
Fiscal Year Ended December 31, 1996

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