Policy and Oversight

Financial and Performance Audit Directorate

Quality Control Review

Coopers & Lybrand, L.L.P.
Ben Franklin Technology Center of Southeastern Pennsylvania
Fiscal Year Ended August 31, 1996

Report Number PO 97-052 September 29, 1997

Office of the Inspector General
Department of Defense

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Acronyms

BFTC	Ben Franklin Technology Center of Southeastern Pennsylvania
OMB	Office of Management and Budget

INSPECTOR GENERAL
DEPARTMENT OF DEFENSE
400 ARMY NAVY DRIVE
ARLINGTON, VIRGINIA 22202-2884

September 29, 1997

Chairman, Non-Profit Industry Group
Coopers & Lybrand L.L.P.
1301 Avenue of the Americas
New York, New York 10019-6013

SUBJECT: Quality Control Review of Coopers & Lybrand L.L.P.
Ben Franklin Technology Center of Southeastern Pennsylvania
Fiscal Year Ended August 31, 1996
Report No. PO 97-052

Introduction

We are providing this report for your information and response. Your Philadelphia, Pennsylvania, office performed the single audit for Ben Franklin Technology Center of Southeastern Pennsylvania (BFTC), Philadelphia, Pennsylvania. BFTC provides assistance to small and new, high-technology companies; joint university and private sector research and development projects for new products and processes; and employment and training programs. The audit is required by the Office of Management and Budget (OMB) Circular A-133, "Audits of Institutions of Higher Education and Other Nonprofit Institutions." BFTC reported total Federal expenditures of $1,251,686 for the fiscal year ended August 31, 1996, representing $930,934 for the Department of Defense and $320,752 for other Federal agencies.

Coopers & Lybrand L.L.P. issued its audit report January 10, 1997, with no findings and no questioned costs. Coopers & Lybrand L.L.P. issued an unqualified opinion on the financial statements, Schedule of Federal Awards, and compliance with specific requirements applicable to major programs. Coopers & Lybrand L.L.P. issued positive and negative assurance statements on compliance with general requirements. Positive assurance states that, with respect to the items tested, the results of the auditors' procedures disclosed no material instances of noncompliance. Negative assurance states that, with respect to the items not tested, nothing came to the auditors' attention that caused them to believe that BFTC had not complied in all material respects. The auditors also obtained an understanding of the internal controls related to

the financial statements and Federal awards. The internal control audit reports describe the auditors' scope of work in obtaining that understanding and in assessing control risk. The report on Federal awards further describes the significant internal controls or control structure, including the controls established to provide reasonable assurance that Federal awards are being managed in compliance with applicable laws and regulations.

Quality Control Review Results

As the Federal oversight agency for the BFTC, we reviewed the audit report for the fiscal year ended August 31, 1996. The audit report is required by Office of Management and Budget Circular A-133, "Audits of Institutions of Higher Education and Other Nonprofit Institutions." The audit met the applicable guidance and regulatory requirements in the OMB Circular A-133, its related Compliance Supplement, Government Auditing Standards, Generally Accepted Auditing Standards, and the provisions of the Federal award agreements, except with regard to substantive testing of major Federal programs. We could not determine if sufficient substantive testing was performed because the sampling plan for performing audit tests of transactions was not documented. As a result, we cannot accept the audit report until this deficiency is corrected.

Sampling Plan Not Documented. The working papers do not document the sampling plan that supports the transaction testing for Federal program compliance. The sampling plan should consist of total universe and sample dollars; universe and sample size; sampling type (judgmental, statistical, etc.); and the criteria for sampling selection. Paragraph 13.c.(3) of the Attachment to OMB Circular A-133 requires that the auditor review an adequate number of transactions from each major Federal program so that the auditor obtains sufficient evidence to support the opinion on compliance. Government Auditing Standards, paragraphs 4.34, 4.35, and 4.37a, require that the auditor document in the working papers the sampling criteria used. The working paper documentation should contain sufficient information to enable an experienced auditor having no previous connection with the audit to determine that the evidence supports the significant conclusions and judgments. Without this type of documentation, those who did not participate in the audit, such as quality control reviewers, cannot understand the auditors' determination of an adequate number of transactions and may conclude that the auditors' opinion on compliance is unsupported. Also, absent documentation concerning the sampling plan, we could not determine if sufficient, competent and revelant evidential matter was collected to support the auditor's opinion.

Recommendation for Corrective Action

We recommend that Coopers & Lybrand L.L.P. document its working papers, in accordance with Government Auditing Standards, for the sampling plans used in the Office of Management and Budget Circular A-133 audit for Ben Franklin Technology Center of Southeastern Pennsylvania for the fiscal year ended August 31, 1996, and provide us a copy of the supporting working paper documentation. If additional transaction testing is required, the auditors should perform the tests, consider the impact of the results, and advise us accordingly.

Quality Control Review Objective

The objective of a quality control review is to assure that the audit was conducted in accordance with applicable standards and meets the auditing requirements of OMB Circular A-133. As the oversight agency for BFTC, we conducted a quality control review of the Coopers & Lybrand L.L.P., audit. Our review focused on the 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, dated September 23, 1994, issued by Ernst and Young L.L.P., which found that Coopers & Lybrand L.L.P. 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 March 31, 1994. Ernst & Young L.L.P. commented on the need to update management representation letters, to tailor the letters to the engagement circumstances, and to comply with the Coopers & Lybrand L.L.P. policies regarding the review of unaudited interim financial information.

Scope and Methodology

We used the 1991 edition of the Uniform Quality Control Guide for Single Audits (the Guide) issued 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. Our review was

conducted on August 25 and September 10, 1997. We reviewed the audit working papers covering all areas of the OMB Circular A-133 audit. About 74 percent of the $1,251,686 in total expenditures relate to the Department of Defense.

Results of Prior Quality Control Reviews

We identified minor quality control review findings and recommendations at 3 of the 10 Coopers & Lybrand L.L.P. locations we visited from January 1, 1995, through June 30, 1997. We notified the affected offices, and no further action is necessary.

Background

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

The Single Audit Act Amendments of 1996, based on 12 years of experience under the 1984 Act, are intended to strengthen the usefulness of single audits by increasing the audit threshold from $100,000 to $300,000 with respect to Federal financial assistance programs before an audit is required under the Act; 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. The Amendments also bring nonprofit organizations, previously covered by similar requirements in the OMB Circular A-133, under the Single Audit Act.

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 carry out 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 revised Circular was issued June 24, 1997, to incorporate the changes in the Single Audit Act Amendments of 1996. Its provisions apply to audits of fiscal years beginning after June 30, 1996.

Discussion of Results

Other than the working papers for the sampling plan, we reviewed and took no exception to the working papers supporting the following reports and schedules.

Independent Accountant's Report on the Basic Financial Statements and Schedule of Federal Awards. The auditor is required to obtain reasonable assurance about whether the financial statements are free of material misstatement. The auditor is also 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. We reviewed the audit program and the testing of evidential matter 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.

Schedule of Federal Financial Assistance. The recipient is responsible for creating the schedule. 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 and reviewed a selected number of footings and cross-footings.

Independent Accountant's Report on the 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 Accountant's Report on the Internal Control Structure Used in Administering Federal Awards. The auditor is required to obtain an understanding of the internal control structure and to assess control risk to determine whether the auditor intends to place reliance on the internal control structure. 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, to 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. We did not retest compliance items in this area.

Independent Accountant's Report on Compliance With Laws, Regulations, Contracts, and Grants Based on an Audit of the Financial Statements Performed 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 Accountant's Report on Compliance With Specific Requirements Applicable to Major Federal Programs. 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. The requirements include 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 that all areas were audited, reviewed the working paper documentation and its support, reviewed the compliance tests performed, and reevaluated selected compliance items.

Independent Accountant'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 auditor's 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.

Comments

Because this report contains a finding and recommendation, written comments are required by November, 28, 1997. We appreciate the courtesies extended during the review. If you have questions on this report, please contact Mrs. Barbara Smolenyak, Program Director, at (703) 604-8761 or Ms. Vera Garrant at (703) 604-8743. See the Enclosure for the report distribution.

Russell A. Rau
Assistant Inspector General
Policy and Oversight

Enclosure

Ben Franklin Technology Center of Southeastern Pennsylvania
Fiscal Year Ended August 31, 1996

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Enclosure

Evaluation Team Members

This report was prepared by the Financial and Performance Audits Directorate, Office of the Assistant Inspector General for Policy and Oversight, DoD.

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