Policy and Oversight

Financial and Performance Audits Directorate

Quality Control Review

Coopers & Lybrand L.L.P.
Woods Hole Oceanographic Institution
Fiscal Year Ended December 31, 1995

Report Number PO 97-027

June 23, 1997

Office of the Inspector General
Department of Defense

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AQI00-05-1285

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Acronyms

DCAA	Defense Contract Audit Agency
OMB	Office of Management and Budget

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June 23, 1997

Chairman, Non-Profit Industry Group
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SUBJECT: Quality Control Review of Coopers & Lybrand L.L.P.
Woods Hole Oceanographic Institution
Fiscal Year Ended December 31, 1995
Report No. PO97-027

Introduction

We are providing this report for your information and use. Your Boston, Massachusetts, suboffice in coordination with the Defense Contract Audit Agency (DCAA) performed the single audit for the Woods Hole Oceanographic Institution (the Institution), Woods Hole, Massachusetts, a not-for-profit research and educational institution. The audit is required by Office of Management and Budget (OMB) Circular A-133, "Audits of Institutions of Higher Education and Other Nonprofit Institutions." The Institution reported total Federal expenditures of $71,897,623 for the fiscal year ended December 31, 1995, representing $25,149,180 for the Department of Defense and $46,748,443 for other Federal agencies.

As the principal auditor, Coopers & Lybrand L.L.P. took full responsibility for the DCAA work in accordance with U.S. Auditing Standards Section 543, "Part of Audit Performed by Other Independent Auditors." As a result, Coopers & Lybrand L.L.P. dual dated its audit report March 29, 1996, and January 27, 1997, to incorporate the DCAA audit results. The auditors questioned $5,737 and issued an unqualified opinion on the financial statements, Schedule of Federal Awards, and compliance with specific requirements applicable to major programs. They 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 the institution has 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 audit reports describe the auditors' scope of work in obtaining that understanding and assessing control risk. The report over Federal awards further describes the significant internal controls or control structure including the controls established that provide reasonable assurance that Federal awards are being managed in compliance with applicable laws and regulations.

Quality Control Review Results

The working papers supporting the OMB Circular A-133 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. The following are suggestions to improve the auditing and reporting processes:

Management Letter Findings. The Coopers & Lybrand L.L.P. electronic working papers must document the management findings identified in the audit report. Currently, these findings are documented as "review notes" in the electronic working papers. However, review notes are purged when the working papers are archived. This information must remain with the working papers to track the findings from the audit report to the working papers and vice versa, to ensure that all findings are reported.

Supporting References to Reports. The DCAA working papers supporting the compliance and internal control reports should contain references to identify the individual working paper packages where the work was performed to evaluate compliance with the common and specific requirements identified in the scope paragraphs of the audit report. The internal control report working paper package only includes references (copies of previously issued reports) to support areas where deficiencies were cited. The compliance and the internal controls working papers do not include the references to the other working paper packages that support the requirements tested. Although Coopers & Lybrand L.L.P. took responsibility for the DCAA audit work, we are forwarding a copy of this report to DCAA for their information and action.

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 the OMB Circular A-133. As the cognizant agency for the Institution, we conducted a quality control review of the audit working papers. 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, performed by Ernst and Young L.L.P. that found that Coopers & Lybrand L.L.P. met the objectives of the quality control review standards established by the American Institution of Certified Public Accountants and the standards were being complied with during the fiscal year ended March 31, 1994. Ernst and Young L.L.P. commented on the need to update management representation letters, to tailor the letters to the engagement circumstances, and to adhere to the Firm's policies regarding the review of unaudited 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. It 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 from May 5 through 15, 1997.

We limited the scope of our quality control review to the Coopers & Lybrand L.L.P. and DCAA audit working papers covering areas related to the Department of Defense expenditures: the financial statements and the research and development program. Coopers & Lybrand L.L.P. took responsibility for the DCAA work; however, we reviewed the DCAA working papers because they represent a significant part of the audit work performed for OMB Circular A-133. The research and development program expenditures were approximately $71.9 million and accounted for nearly 100 percent of total Federal award expenditures.

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 December 31, 1996. The affected offices were notified 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 these 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; selecting programs to be audited on the basis of risk assessment rather than the amount of dollars involved; and improving the contents and timeliness of single audits. The Amendments also bring nonprofit organizations, previously covered by similar requirements under the OMB Circular A-133, under the Single Audit Act.

The OMB Circular A-133, "Audits of Institutions of Higher Education and Other Nonprofit Institutions," 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. It 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 Circular is currently being revised to incorporate the changes in the Single Audit Act Amendments of 1996.

Discussion of Results

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

Report of Independent Accountants. 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 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.

Report of Independent Accountants on Supplementary Information: Schedule of Federal Award Expenditures. The auditor is required to subject the schedule 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 "Report of Independent Accountants."

Schedule of Federal Award Expenditures. 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, reviewed a selected number of footings/cross-footings, and traced some of the amounts to the Subsidiary Ledger and/or Trial Balance.

Report of Independent Accountants on the Internal Control Structure Based on an Audit of Financial Statement Performed 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 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.

Report of Independent Accountants on the Internal Control Structure Used in Administering Federal Awards. The auditor is required to obtain an understanding of the internal control structure and 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 non-compliance, review the system for monitoring subrecipients and obtaining and acting on subrecipient audit reports, and determine whether controls are effective to ensure direct and indirect costs are computed and billed in accordance with the requirements in the compliance

supplement. We reviewed the Coopers & Lybrand L.L.P. and DCAA audit programs for the appropriate procedures, the working paper documentation, and the test of controls performed and re-evaluated selected internal control items.

Report of Independent Accountants on Compliance With Laws, Regulations, Contracts, and Grants Based on an Audit of 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.

Report of Independent Accountants on Compliance With Specific Requirements Applicable to Major 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. They 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 all areas are audited, reviewed the working paper documentation and its support, reviewed the compliance tests performed, and re-evaluated selected compliance items.

Report of Independent Accountants on Compliance With General Requirements Applicable to Federal Assistance 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. 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 Compliance Supplement for "Audits of Institutions of Higher Learning and Other Non-Profit Institutions." We reviewed the audit program for the appropriate procedures, compared the audit program steps to those in the Compliance Supplement to make sure all areas are audited, reviewed the working paper documentation and its support, reviewed the compliance tests performed, and re-evaluated selected compliance items.

Schedule of Reportable Conditions, Current and Prior Years. The auditor is required to identify in the audit report the reportable conditions, including material weaknesses found as a result of the auditor's work in understanding and assessing the control risk. We traced the reportable conditions in the working papers to the audit report to make sure that the report includes all reportable

conditions identified in the working papers and that the reportable conditions are properly supported. The reportable conditions are provided in Enclosure 1.

Schedule of Findings and Questioned Costs. The auditor is required to report material findings of noncompliance in the audit report in their proper perspective: the size of the universe in number of items and dollars, the number and dollar amount of transactions tested by the auditors, and the number and corresponding dollar amount of instances of noncompliance. We traced the $5,737 questioned cost in the DCAA working papers and the insurance and filing findings in the Coopers & Lybrand L.L.P. working papers to the audit report to make sure that the report included all current year findings identified in the working papers and that the findings were properly supported. We also traced the prior year's findings in the working papers to the audit report (Enclosure 1).

Management Letter Comments. The auditor uses the management letter to inform top level management about other concerns raised during the audit that do not effect the report opinions. These suggestions are usually aimed at improving operational processes but have also been expanded to include immaterial findings based on an audit in accordance with OMB Circular A-133. Coopers & Lybrand L.L.P. issued a management letter dated April 22, 1996, to the Institution's Audit Committee addressing recommendations to improve the conversion of the general ledger and purchasing function to the new BiTech System. We traced the recommendations in the working papers to the management letter to make sure that the management letter includes all recommendations identified in the working papers. The recommendations and immaterial findings, including 1994 findings not fully addressed, are presented in Enclosure 1.

Comments

Since this report contains no findings or recommendations, written comments are not required. We appreciate the courtesies extended during the review. If you have questions on this report, please contact Mr. Donald Steele, Project Manager, at (703) 604-8705 or Ms. Vera Garrant at (703) 604-8743. See Enclosure 2 for the report distribution.

Russell A. Rau
Assistant Inspector General
Policy and Oversight

Enclosures

Woods Hole Oceanographic Institution
Fiscal Year Ended December 31, 1995

Schedule of Reportable Conditions, Findings, and Questioned Costs

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	Reportable Conditions:	
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33	Time and Effort System	ONR
34	Graduate Research Assistance Costs on NOAA Grants	ONR
35	Cost Sharing	ONR*
35	Subcontracts	ONR*
	Findings & Questioned Costs:	
41	Indirect Costs Charged Direct for Graduate Research Assistance Costs on NOAA Grants ($5,737)	ONR
42	Insurance and Bonding	ONR
42	Filing of Technical Report and Contract Close Outs	ONR
	Management Letter Comments & Observations (Current Year):	
	A. New BiTech System Implementation Project & Related Staff User Access Employee Termination Firewalls Application Ids & Passwords Dial-Up Activity Physical Security Defined Policies & Procedures Change Management Policies Business Continuity Planning	ONR
	B. Observation: System Impact of the Year 2000	N/A

Woods Hole Oceanographic Institution
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Schedule of Reportable Conditions, Findings, and Questioned Costs

Page #	Title	Agency
	Management Letter Comments & Observations (Prior Year):	
	Contracts and Grants	ONR*
	Billing	ONR*
	Employee Benefit Plan Management	ONR*
	Cash Management	ONR*
	Reorganization / System Implementation	ONR*
	Investment Manager & Other Contract Review	ONR*
	Implementation of New Information System	ONR*

*Resolved in current year or has been partially addressed.

ONR Office of Naval Research
NOAA National Oceanic and Atmospheric Administration

Woods Hole Oceanographic Institution
Fiscal Year Ended December 31, 1995

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Enclosure 2

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

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A. Report Title Coopers & Lybrand L.L.P. Woods Hole Oceanographic Institution Fiscal Year Ended December 31, 1995

B. DATE Report Downloaded From the Internet: 02/28/99

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D. Currently Applicable Classification Level: Unclassified

E. Distribution Statement A: Approved for Public Release

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