

*O*versight

*R*eport



QUALITY CONTROL REVIEW OF PRICEWATERHOUSECOOPERS,
LLP, FOR OMB CIRCULAR A-133 AUDIT REPORT OF INSTITUTE
FOR DEFENSE ANALYSES, FISCAL YEAR ENDED
SEPTEMBER 25, 1998

Report Number D-2000-6-008

August 14, 2000

Office of the Inspector General
Department of Defense

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Acronyms

AICPA	American Institute of Certified Public Accountants
CPE	Continuing Professional Education
DCAA	Defense Contract Audit Agency
GAGAS	Generally accepted government auditing standards
IDA	Institute for Defense Analyses
OMB	Office of Management and Budget
PwC	PricewaterhouseCoopers, LLP



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

August 14, 2000

Treasurer
Institute for Defense Analyses

Partner
PricewaterhouseCoopers

SUBJECT: Report on Quality Control Review of
PricewaterhouseCoopers, LLP, for OMB Circular A-133 Audit Report of
Institute for Defense Analyses, Fiscal Year Ended September 25, 1998
Report No. D-2000-6-008 (Project No. D2000-OA-0123)

We are providing the report for information and use. The Institute for Defense Analyses engaged the PricewaterhouseCoopers, LLP, McLean, Virginia, to perform the audit that is required by the Office of Management and Budget Circular A-133 (the Circular), "Audits of States, Local Governments, and Non-Profit Organizations," dated June 24, 1997 (also referred to as "the single audit"). The Institute for Defense Analyses is a non-profit corporation that operates as a federally funded research and development center based in Alexandria, Virginia. For the fiscal year ended September 25, 1998, the Institute for Defense Analyses reported total Federal expenditures of \$109,951,862 for two DoD contracts.

Background. On December 4, 1998, PricewaterhouseCoopers, LLP, (PwC) issued their single audit report containing unqualified opinions on the financial statements, the Schedule of Expenditures of Federal Awards, and the compliance with requirements applicable to the Federal contracts at the Institute for Defense Analyses (IDA). In addition, PwC provided reports on internal control over financial reporting and over compliance and prepared a Schedule of Findings and Questioned Costs that summarizes the results of the single audit. The Defense Contract Audit Agency (DCAA), Alexandria, Virginia, also submitted a report dated October 1, 1999, as required by the Circular, that duplicated PwC reporting on internal control over compliance; related opinions on compliance of major contracts with laws, regulations and the contract provisions and the Schedule of Expenditures of Federal Awards; and a Schedule of Findings and Questioned Costs. In contrast to PwC, DCAA described internal control weaknesses that they considered reportable but not material and one instance of noncompliance with the Allowable Costs/Cost Principles requirement

Quality Control Review Objective. As the cognizant agency for IDA, the Office of Inspector General, DoD, performed a quality control review of the Office of Management and Budget (OMB) Circular A-133 Single Audit of IDA for the fiscal year ended September 25, 1998

The objective of our review was to determine whether the FY 1998 report that IDA submitted to the Single Audit Clearinghouse met the applicable reporting standards and whether PwC conducted the audit as required by applicable standards and the Circular. See Appendix A for a discussion of the scope, prior quality control reviews related to PwC, and single audit requirements.

Review Results. PwC complied with the Circular in performing the audit of the financial statements and reporting on compliance and on internal control over financial reporting. However, PwC did not meet the requirements of the Circular that related to the review of compliance with requirements and internal control over compliance because the FY 1998 single audit was not adequately planned, executed, and documented (see finding A). Moreover, IDA did not properly coordinate the single audit between the DCAA and PwC, whose organizations, in turn, did not take appropriate steps to consider each other's work to achieve a proper review of all matters (see finding B).

Finding A. Performance of Fiscal Year 1998 Single Audit. As required by the Circular, PwC provided a complete reporting package that IDA submitted to the Single Audit Clearinghouse. In addition, PwC adequately performed the audit of the financial statements. However, PwC did not adequately plan the audit of internal control over compliance with requirements; therefore, the testing of the internal control and compliance requirements were improperly executed. The inadequacies occurred, in part, because PwC used an outdated audit program. Also, documentation was limited or non-existent for the audit as a whole. PwC did not consider the risk associated with using computer imagery at IDA for record retention. Because the compliance audit was not performed according to the Circular, the costs incurred by IDA for the single audit services are unallowable.

Review of Internal Control Over Compliance. PwC did not adequately plan the review of internal control for the one major program at IDA, research and development. The Circular, generally accepted government auditing standards (GAGAS), and the American Institute of Certified Public Accountants (AICPA) guidance on generally accepted auditing standards require that the audit be properly planned to identify and test the internal control for each major program. The auditors must first identify which of the 14 compliance requirements can be applied to the major program at IDA. Then the audit working papers should indicate a sufficient understanding of internal control over Federal programs by evaluating how the five elements of internal control--control environment, risk assessment, control activities, information and communication, and monitoring--related to each applicable compliance requirement. The auditors should use the understanding of the internal control they documented to (1) identify types of potential noncompliance, (2) consider factors affecting the risk of material noncompliance, and (3) design compliance tests.

PwC failed to adequately test internal control and plan the compliance review because they did not properly identify the applicable 14 compliance requirements and assess the related internal control. The following table shows which of the 14 compliance requirements PwC determined to be applicable and the testing of internal control as reflected in the PwC working papers.

Determination of Applicability of Compliance Requirements by PwC

<u>Compliance Requirement</u>	<u>Determined to be Applicable by PwC*</u>	<u>Internal Control Tested by PwC</u>
A. Activities Allowed or Unallowed	X	
B. Allowable Costs/Cost Principles	X	
C. Cash Management	N/A	
D. Davis-Bacon Act	N/A	
E. Eligibility of Federal Funds	N/A	
F. Equipment and Real Property Management	X	
G. Matching, Level of Effort, Earmarking	N/A	
H. Period of Availability of Federal Funds	X	
I. Procurement and Suspension and Debarment	X	X
J. Program Income	N/A	
K. Real Property Acquisition/Relocation Assistance	N/A	
L. Reporting	X	
M. Subrecipient Monitoring	N/A	
N. Special Tests and Provisions	--	

* The PwC working papers showed that the compliance requirement was applicable ("X") or not applicable ("N/A") to the research and development program, and, in one case, was not considered ("--") as to its applicability at IDA.

The PwC working papers do not indicate how the auditors determined which of the 14 compliance requirements were applicable and to what extent they were applicable to IDA. PwC determined that 7 of the 14 compliance requirements were not applicable to IDA. However, Item G, "Matching, Level of Effort, Earmarking," is applicable. PwC did not obtain sufficient evidence to know whether the item applied to IDA. IDA has contracts with level-of-effort requirements. PwC indicated that they had reviewed abstracts or briefs of the original contracts. However, in the working papers, PwC did not refer to nor include copies of the contracts, abstracts, or contract briefs to support their consideration of the compliance requirement.

For the six compliance requirements that PwC determined to be applicable, the working papers do not show the assessment of internal control for each applicable compliance requirement. PwC tested the internal control for only one of the compliance requirements. For Item I, "Procurement and Suspension and Debarment," PwC documented that IDA had written policies and procedures and selected the item as the only area for testing the operation of internal control over compliance. We attempted to re-test the original five vouchers selected by PwC for mathematical accuracy, approval, and allowability. We could find only three vouchers, which were all for travel and not procurements. The working papers show no criteria to measure for allowability, and no value, descriptions of transactions, conclusions or results of testing. According to the working papers, the vouchers were tested for an internal

control feature of “approval,” and although one of the three travel vouchers did not have the proper signature for approval, it was still paid. To add to the deficiency of the test, PwC did not review the major element of Compliance Requirement Item I that ensures that purchases of goods or services are not procured from any debarred or suspended entity.

For Item L, “Reporting,” PwC working papers identified one report required of IDA--Standard Form 1034, a public voucher (an IDA payment vehicle). PwC did not address the internal control that would identify the accounting or performance records to support the payments. In a subsequent step of the audit, PwC addressed additional contract reports that were not considered in the assessment of internal control over the compliance for “Reporting.” For Item N, “Special Tests and Provisions,” the PwC working papers do not show any assessment of this compliance requirement.

For the assessment of all compliance requirements, PwC failed to consider four DCAA audit reports, in which each addressed a major component of the IDA accounting system including the control environment and overall accounting system controls, labor accounting system, billing system, and the accounting system for indirect and other direct costs. Each report concluded that the system is inadequate, in part, based on the lack of written policies and procedures. PwC did not document any reference to these internal control weaknesses in their assessment or resolve the DCAA consideration of these deficiencies as a “reportable condition,” as defined by the AICPA.

The auditors used an audit program that was developed before the OMB Circular A-133, dated June 24, 1997, was revised. The audit program was not designed to review the five elements of internal control for each compliance requirement of the AICPA Statement of Position 98-3, “Audits of States, Local Governments and Not-for-Profit Organizations Receiving Federal Awards.” The working papers had no evidence of the assessment of internal control over the applicable compliance requirements for the audit steps in their audit program. The deficient review of internal control over compliance does not provide a sound basis for the compliance review of the two multi-year, multi-million dollar contracts representing the FY 1998 Federal expenditures of \$109,951,862.

Audit Execution and Documentation. The PwC working papers do not demonstrate the review and tests of internal control and compliance requirements to support the opinion on compliance. GAGAS require that the form and content of the working papers should allow an experienced auditor to understand the auditor’s 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, perform the same analyses, and come to the same conclusions. PwC reviewed costs for the 2 major contracts at IDA by testing 15 transactions from each contract. The working papers do not show the type of cost element, its amount, date/time period, or what specific criteria were used to determine the allowability of any transaction. We reviewed additional information from PwC to re-test a sample of the transactions, but the spreadsheet provided no additional

clarification of the testing conducted by PwC. The inadequate explanations in the working papers provide no audit trail and no reasonable assurance that IDA materially complied with the compliance requirements.

Compliance testing includes the examination of transactions and other auditing procedures that provide the auditors with sufficient evidence to support an opinion on compliance, required by Part 3 of the A-133 Compliance Supplement. The PwC working papers do not show what was tested and how the test was conducted. A PwC working paper that tests Compliance Requirement Item L, "Reporting" explains that three different types of reports "appear to have been forwarded to the appropriate contracting officer." The same working paper does not refer to the public voucher that PwC identified as the only report to support the applicability of Item L (refer to the previous discussion in the "Review of Internal Control Over Compliance" subparagraph). Throughout the working papers, PwC consistently referred to the contracts as "grants" and did not refer to the specified cost principles of the Federal Acquisition Regulation as a criteria for measuring compliance for the federally funded research and development center, even when reviewing Compliance Requirement Item B, "Allowable Costs/Cost Principles." Their permanent files contained one copied portion of the Federal Acquisition Regulation that referenced section 31.205-18, "Independent research and development and bid and proposal costs." PwC did not demonstrate in their working papers that their audit steps had been thorough and conclusive.

Audit Coverage of Computer Imagery for Retention of Records. PwC informed us that they reviewed electronic images of the vouchers from the contractor's electronic record scanning system in all transaction testing. They had not assessed the system for reliable input/output and maintenance of original documentation according to the Federal Acquisition Regulation 4.703, "Policy [for Contractor Records Retention]." Therefore, without an assessment of the computer-generated documentation, PwC should have reviewed original documentation. The hard copy documentation would have been available during their review, since they conducted their fieldwork immediately following the end of the fiscal year, and the contractor maintains the original documentation for one year after it is scanned.

DCAA had reviewed the electronic record scanning system and reported in May 1997 that it was inadequate, in part, due to the lack of written policies and procedures. However, DCAA did not provide the audit information to PwC. Based on their review, DCAA indicated that they would need to continue reviewing, on a selective basis, the hard copy documentation until IDA had formally submitted their policies and procedures. The audit organizations need to verify the scanned documents to the original records to ensure integrity of the contractor's underlying documentation.

Auditor Qualifications. The PwC audit program, Step 28, included a cautionary note to "ensure that all members of the engagement have met the minimum CPE requirements contained in the Yellow Book and document this fact in the planning memorandum." The working papers did not address this program step. The CPE requirements under Paragraph 3.6 in GAGAS include at least 80 hours of continuing education and training, which contributes to the auditor's professional proficiency every

2 years, at least 20 hours of which should be completed in any 1 year of the 2-year period. GAGAS also requires auditors responsible for auditing under these standards to complete at least 24 of the 80 hours of continuing education and training in subjects directly related to the government environment and to government auditing. In addition, auditors should receive training that is specifically related to any audited entity operating in a unique environment such as IDA.

Responsibility of IDA for PwC Audit. Our review of the PwC FY 1998 single audit concludes that the audit does not meet the requirements of OMB Circular A-133. IDA paid PwC a total of \$79,573.29 to perform the FY 1998 single audit by IDA. OMB Circular A-133 §____. 230(b)(1) does not allow a non-Federal entity to charge the cost of any audit under the Single Audit Act Amendments of 1996 that was not conducted according to the Circular. Therefore, any costs originally incurred for audit services billed by PwC for the FY 1998 single audit must be accumulated separately as unallowable costs and must not be charged to Federal awards until the audit is corrected. IDA should require PwC to properly perform the audit at no additional cost to the government.

Summary. The auditors did not adequately plan, execute, and document the compliance part of the single audit according to the OMB Circular A-133 requirements. As a result, there is no basis to rely on the internal control to plan and execute the compliance tests. Considering the FY 1998 deficiencies, IDA needs to ensure that future single audits meet the Circular requirements. Federal agencies need to be able to rely on the audit report's assurance that internal control procedures are in place and operating effectively for the major programs that are identified in the audit report and that there is a reliable basis for the opinion rendered on the compliance for IDA.

Recommendations, and Management Comments

A.1. We recommend that the Treasurer, Institute for Defense Analyses:

a. **Require that PricewaterhouseCoopers, LLP, redo the audit of the Institute for Defense Analyses for its fiscal year ended September 25, 1998, according to the Office of Management and Budget Circular A-133 and at no additional cost to the Federal Government.**

PwC Comments. The PwC management concurred for IDA who agrees with the comments provided by PwC. The management comments (see page 15) include correction plans to withdraw their audits to redefine the scope of audit and revise the reporting package required by the OMB Circular A-133 to include the audit work of DCAA.

b. **Identify as unallowable any costs associated with audit services that were originally provided by PricewaterhouseCoopers, LLP, to report on the Fiscal Year 1998 single audit until the audit is corrected according to the Office of Management and Budget Circular A-133.**

PwC Comments. The PwC management concurred for IDA who agrees with the comments provided by PwC. PwC intends to credit IDA for an estimated \$17,000 of their original fee for the subject audit.

c. **Ensure that deficiencies identified in the Fiscal Year 1998 audit are not repeated in the Fiscal Year 1999 and future single audits.**

PwC Comments. The PwC management concurred for IDA who agrees with the comments provided by PwC. PwC stated that they plan to correct the Fiscal Year 1999 single audit in the same manner they are addressing Fiscal Year 1998 and will continue the same approach to the single audit for future years.

A.2. We recommend that PricewaterhouseCoopers, LLP:

a. **Document in the working papers its judgments, procedures, and results or conclusions with relevant and sufficient evidence for all audit steps.**

b. **Revise its audit program for the single audit to comply with the requirements of Office of Management and Budget Circular A-133 to include audit steps that document an understanding of the 5 internal control elements related to each of the applicable 14 compliance requirements.**

c. **Coordinate and document their audit effort with Federal auditors, throughout the conduct of the single audit according to the Office of Management and Budget Circular A-133.**

d. Obtain training to ensure that the staff assigned to the Office of Management and Budget Circular A-133 audits is properly trained.

e. Adhere to its audit program step for the single audit that requires continuing professional education for all auditors assigned to the engagement be documented in the working papers.

PwC Comments. PwC concurred with recommendations A.2.a. through e and proposed acceptable corrective actions.

Finding B. Coordination of Single Audit. The IDA did not ensure that the single audit required by the Circular was properly coordinated between PwC and DCAA. PwC and DCAA did not take appropriate steps to properly review all matters relating to the single audit.

Procuring Single Audit Services. In July 1998, IDA engaged PwC to provide all FY 1998 audit services required to meet the intent of the Circular. However, DCAA maintains an on-site suboffice at IDA that provided an annual average of 1600 hours of contract audit services from FY 1996 through 1998. The contract audit services supported DoD procurement and contract administration activities and included reviews of certified submissions for each fiscal year's incurred costs and their compliance with requirements identified in the Circular. In March 1997, after a meeting with PwC and IDA concerning the requirements of the Circular, DCAA provided PwC (through IDA) with an audit matrix showing a proposed division of responsibility between DCAA and PwC for the FY 1998 single audit. Aside from the requirements of the OMB Circular A-133 § ___.305 "Auditor selection," IDA did not consider the services provided by the DCAA in arranging for PwC to complete the single audit as shown in the engagement letter dated July 31, 1998. In order to achieve a more cost-effective audit, IDA must recognize their responsibility in coordinating the single audit as required by the Circular.

Relying on Work Performed by Other Auditors. According to PwC, except for the March 1997 meeting, they did not coordinate with or contact DCAA before or during the FY 1998 single audit. The PwC single audit report does not mention relying on DCAA, nor does it recognize their audit efforts. However, our review of the PwC working papers shows that during their review, they requested and IDA provided copies of four separate DCAA audit reports, in which each addressed a major system including the control environment and overall accounting system controls, labor accounting system, billing system, and the accounting system for indirect and other direct costs. Each audit concluded that the IDA systems were inadequate in part, based on the absence of written policies and procedures for each system. The PwC working papers had no evidence as to how they addressed the system deficiencies. DCAA considered the system deficiencies a reportable condition in their A-133 audit as addressed by the Circular. DCAA also provided their annual program plan and a list of audits in progress through IDA to PwC. Generally accepted auditing standards state that when part of the audit is performed by other auditors:

The principal auditor may also need to refer to the programs audited by other auditors in his or her reports on the schedule of expenditures of federal awards, compliance, and internal control related to federal awards, as they relate to federal awards administered by the component unit. In such cases, the auditor should follow the guidance in SAS [Statement on Auditing Standards] No. 1, section 543 ["Part of Audit Performed by Other Independent Auditors"]

Clearly, PwC was aware of DCAA, their audit plans, and audit reports. The OMB Circular A-133 § ___.215 "Relation to other audit requirements" requires that "(a)ny additional audits shall be planned and performed in such a way as to build upon work performed by other auditors." PwC should be coordinating with DCAA to achieve a complete and cost-effective review of the Federal awards.

If IDA had obtained a coordinated audit, the auditors could have relied on the work of others in completing the audit. In order to achieve a more cost-effective audit, IDA, PwC, and DCAA must all recognize their individual responsibilities in coordinating the single audit.

Recommendation and Management Comment

B. We recommend that the Treasurer, Institute for Defense Analyses, ensure a coordinated audit among the procured services of the independent public accountant and the Defense Contract Audit Agency to avoid duplication, and to achieve a complete and cost effective audit.

IDA Response. IDA concurs. IDA did not provide a formal written response but their correction plan is in progress as evidenced by a coordination meeting established for the FY 2000 single audit with PwC, DCAA, and the OIG, DoD.

We appreciate the courtesies extended during the review. If you have questions on this report, please contact Mr. Wayne C. Berry at (703) 604-8789 (wberry@dodig.osd.mil) or Ms. Joanne Wallis at (703) 604-8748 (jwallis@dodig.osd.mil). The report distribution is at Appendix B. The audit team members are listed inside the back cover.



Patricia A. Brannin
Deputy Assistant Inspector General
for Audit Policy and Oversight

Appendix A. Quality Control Review Process

Scope and Methodology

We conducted a quality control review of the PricewaterhouseCoopers, LLP, audit of the Institute for Defense Analyses (IDA) for the fiscal year ended September 25, 1998, and the resulting reporting submission to the Single Audit Clearinghouse dated March 1, 1999. We performed our review using the 1999 edition of the “Uniform Quality Control Guide for the A-133 Audits” (hereafter referred to as “the Guide”). The Guide applies to any single audit that is subject to the requirements of Office of Management and Budget (OMB) Circular A-133, revised June 24, 1997. The Guide is the approved checklist of the President’s Council on Integrity and Efficiency for performing the quality control review procedures. We reviewed the audit as required by the OMB A-133 Circular, generally accepted government auditing standards issued by the Comptroller General of the United States, and generally accepted auditing standards issued by the American Institute of Certified Public Accountants. Our review was conducted from December 1999 through June 2000 and covered areas related to the financial statements and the one major program, research and development. As the cognizant audit agency for IDA, we focused our review on the following qualitative aspects of the single audit:

- Qualifications of auditors
- Independence
- Due professional care
- Quality control
- Planning and supervision
- Internal control and compliance testing
- Schedule of Expenditures of Federal Awards
- Schedule of Findings and Questioned Costs
- Data Collection Form

Prior Quality Control Reviews

Since January 1997, we have performed 10 quality control reviews of Coopers & Lybrand, 1 quality control review of Pricewaterhouse, and 3 quality control reviews of PricewaterhouseCoopers. In 3 of the 14 reports, we identified 4 deficiencies resulting in findings and made recommendations. In addition, 3 of the 14 reports contained 7 conditions that were reported and suggestions made for improvements.

Single Audit Requirements

In June 1997, the OMB issued Circular A-133, "Audits of States, Local Governments, and Non-Profit Organizations." The Circular establishes policies to guide implementation of the Single Audit Act 1996 (Public Law 98-502) amendments and provides an administrative foundation for uniform audit requirements for non-Federal entities that administer Federal awards. In addition, the Circular serves to ensure that Federal departments and agencies rely on and use the audit work to the maximum extent practicable. To meet the intent of the law and the Circular, a complete reporting package on each single audit is submitted to the Single Audit Clearinghouse from the auditee (non-Federal entity) that includes the following:

- Data collection form certified by the auditee that the audit was completed according to the OMB Circular A-133;
- Financial statements and related opinion;
- Schedule of Expenditures of Federal Awards and related opinion;
- Report on internal control and compliance review related to the financial statements;
- Report on internal control over compliance and on compliance with laws, regulations, and the provisions of contracts or grant agreements, and related opinion on compliance of major programs; and
- Schedule of Findings and Questioned Costs.

OMB issues an annual Compliance Supplement that assists the auditors in determining the audit scope for the Circular's requirements for review of internal control. 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 five components of internal control (control environment, risk assessment, control activities, information and communication, and monitoring) for each compliance requirement. The following 14 compliance requirements applicable to the various Federal programs are identified in the Supplement:

- | | | | |
|----|--|----|---|
| A. | Activities Allowed/Unallowed | H. | Period of Availability of Federal Funds |
| B. | Allowable Costs/Cost Principles | I. | Procurement and Suspension and Debarment |
| C. | Cash Management | J. | Program Income |
| D. | Davis-Bacon Act | K. | Real Property Acquisition/Relocation Assistance |
| E. | Eligibility of Federal Funds | L. | Reporting |
| F. | Equipment and Real Property Management | M. | Subrecipient Monitoring |
| G. | Matching, Level of Effort, Earmarking | N. | Special Tests and Provisions |

Appendix B. Report Distribution

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PricewaterhouseCoopers, LLP, Comments



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31 July 2000

**Subject: Comments on Draft Discussion Draft
Project No. D2000-OA-0123
Institute for Defense Analyses (IDA)**

Dear Ms Brannin:

Thank you for the opportunity to respond to the discussion draft of your quality control review of the PwC OMB Circular A-133 audit of IDA for the fiscal year ended September 25, 1998. We appreciate the time Mr Berry and Ms Wallis spent with us reviewing this draft and making suggestions for the development of the action plan discussed below.

In particular, we appreciate their providing to us a copy of the Defense Contract Audit Agency (DCAA) audit report No 6121-1999H10160001 dated October 1, 1999 on its Circular A-133 audit of IDA for the year ended September 25, 1998. While our client had received a draft of the DCAA audit report, we were not aware of this report. As we have discussed with Mr Berry and Ms Wallis, communications could be enhanced among us, our client, and the DCAA.

As suggested in your discussion draft, much of the work the DCAA and we performed was, with hindsight, duplicative. The DCAA performed an audit under OMB Circular A-133 solely as it pertains to applicable compliance requirements of federal awards.

Ms Patricia A Brannin
July 31, 2000
Page 2

We issued a complete OMB Circular A-133 report covering both the financial statements and applicable compliance requirements of federal awards. The duplication of effort with respect to federal awards is unnecessary under the "co-ordination of effort" concept encouraged by the Circular.

Action Plan

As we discussed with Mr. Berry and Ms. Wallis, we propose to co-ordinate our work more thoroughly with DCAA on both a prospective and a retroactive basis. Based on conversations we are currently having with DCAA, we plan to withdraw and attempt to recover all copies of our 1998 OMB Circular A-133 report on federal awards. Under this plan we will revise the Single Audit reporting package required by paragraph 320 c of OMB Circular A-133 to reflect the portions of the OMB Circular A-133 audit performed by our firm and DCAA. This action will also necessitate a re-filing of IDA's 1998 data collection form with the Single Audit Clearing House. The details of these actions are currently being worked out with DCAA.

We also plan to credit our client with a portion of the incremental audit fee for the 1998 A-133 audit report. We estimate that credit will approximate \$17,000.

Going forward (including 1999), we plan to continue this division of audit effort to the extent we can arrive at a mutual agreement with DCAA. Both organizations have agreed that should it become necessary to support one another in our individual efforts, we will do so.

This proposed action resolves in an effective and efficient way most of the recommendations included in your discussion draft for both us and IDA. As noted in the attachment to this letter, many of the recommendations will be addressed in future audits. The IDA responses in the attachment have been reviewed with our client who concurs with the responses. Furthermore, the preparation of this correspondence was coordinated with Mr. Berry and Ms. Wallis.

OIG Recommendations and Response

OIG Recommendation	Response
For PwC:	
a Document in the working papers judgments, procedures, and results or conclusions with relevant and sufficient evidence for all audit steps	a This recommendation pertains to federal award work since the discussion draft did not question our audit of the financial statements. In the future, we will ensure that the working papers clearly document judgements, procedures and results or conclusions with evidence of all steps. As it relates to the 1998 audit of IDA, the DCAA audit report covers all applicable compliance requirements for federal awards.
b Revise audit programs for single audit to comply with the requirements of OMB Circular A-133 to include audit steps that document an understanding of the 5 internal control elements related to each of the 14 compliance requirements	b With respect to our practice overall, we have taken and continue to take steps to introduce new electronic audit program and continuing professional education on these matters. The revised audit program will be tailored as appropriate for IDA to comply with all requirements of OMB Circular A-133 related to internal control.
c Coordinate and document audit effort with Federal auditors, throughout the conduct of the single audit according to OMB Circular A-133.	c The Action Plan discussed in our letter satisfies this recommendation.
d Obtain training to ensure the staff assigned to the OMB Circular A-133 audits is properly trained	d We have and will continue to do so in the future. Attached is documentation of the 1998 audit staff's compliance with the CPE requirements of GAGAS for financial statement audit purposes.
e Adhere to its audit program step for the single audit that requires continuing professional education for all audits assigned to the engagement be documented in the working papers	e In the future, we will include such documentation in the working papers.
For IDA	
a Require that PwC redo the audit of IDA for its fiscal year ended September 25, 1998 according to OMB Circular A-133 and at no additional cost to the Federal Government.	a The Action Plan described in the PwC letter achieves the desired result in an effective and efficient manner.
b Identify as unallowable any costs associated with audit services that were originally provided by PwC to report on the Fiscal Year 1998 single audit until the audit is corrected in accordance with OMB Circular A-133.	b The Action Plan described in the PwC letter achieves the desired result in an effective and efficient manner.
Ensure that deficiencies identified in the Fiscal Year 1998 audit are not repeated in the Fiscal Year 1999 and future single audits.	c The Action Plan described in the PwC letter achieves the desired result in an effective and efficient manner.

Evaluation Team Members

This report was prepared by the Deputy Assistant Inspector General for Audit Policy and Oversight, Office of the Assistant Inspector General for Auditing, DoD.

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