

*O*versight

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REPORT ON QUALITY CONTROL REVIEW OF
GRANT THORNTON LLP, FOR
OFFICE OF MANAGEMENT AND BUDGET
CIRCULAR NO. A-133 AUDIT REPORT OF
CONCURRENT TECHNOLOGIES CORPORATION
FISCAL YEAR ENDED JUNE 30, 1998

Report Number D-2001-6-002

February 23, 2001

Office of the Inspector General
Department of Defense

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Acronym

ACO	Administrative Contracting Officer
CTC	Concurrent Technologies Corporation
DCAA	Defense Contract Audit Agency
GAS	Government Auditing Standards
OMB	Office of Management and Budget

February 23, 2001

Executive Director and Treasurer
Concurrent Technologies Corporation

Partner-in-Charge
Grant Thornton, LLP

Director
Defense Contract Management Agency

SUBJECT: Report on Quality Control Review of Grant Thornton LLP,
for Office of Management and Budget Circular A-133
Audit Report of Concurrent Technologies Corporation,
Fiscal Year Ended June 30, 1998
Report No. D2001-6-002 (Project No. D2000-OA-0150)

We are providing this report for your review and comment. The firm of Grant Thornton, LLP (Grant Thornton), performed the single audit for the Concurrent Technologies Corporation (CTC), an independent non-profit organization based in Johnstown, Pennsylvania. Grant Thornton partially relied on the audit work of Wessel & Company and the Defense Contract Audit Agency (DCAA) in completing its audit. The audit is required by Office of Management and Budget (OMB) Circular A-133, "Audits of States, Local Governments, and Non-Profit Organizations" (hereafter called Circular A-133). For the fiscal year ended June 30, 1998, CTC expended approximately \$92.8 million against Federal awards, representing \$90.3 million for the DoD and \$2.5 million for other Federal agencies.

Quality Control Review Objective. As the cognizant agency for CTC, the Office of Inspector General, DoD, performed a quality control review of the FY 1998 audit to determine whether the audit report that CTC submitted to the Single Audit Clearinghouse met the applicable reporting standards and whether Grant Thornton conducted the audit in accordance with applicable standards and Circular A-133. See Appendix A for a discussion of the scope and single audit requirements.

Review Results. Grant Thornton generally complied with applicable auditing standards and the requirements contained in Circular A-133 and its related Compliance Supplement for the Research and Development program. However, we identified

deficiencies relating to reporting and documentation requirements. As a result of our review, Grant Thornton addressed these deficiencies (finding A). In addition, CTC charged unallowable audit costs to the Federal Government for audit services (see finding B). Moreover, CTC did not comply with Circular A-133 requirements because the original reporting package did not include a Summary Schedule of Prior Audit Findings (see finding C).

Finding A. Performance of the Fiscal Year 1998 Single Audit. Grant Thornton working papers supporting the audit of internal control over compliance and the audit of compliance with major program requirements did not meet GAS documentation requirements. In addition, the auditor's report on the financial statements did not include the required reference to GAS, and the Schedule of Findings and Questioned Costs did not include all audit findings.

Working Paper Documentation. The working papers did not clearly document the procedures performed to accomplish the objectives of Circular A-133 requirements for an audit of major Federal programs. The lack of clear documentation occurred in part because the auditors relied on work performed in the financial statement audit as a basis for fulfilling the requirements of the Federal program audit. However, they did not prepare working papers to draw the relationship between the procedures performed on the financial statement audit and Circular A-133 objectives being tested.

Specifically the working papers did not clearly document:

- the auditor's determination of applicable and material compliance requirements;
- the auditor's understanding of internal control over certain applicable compliance requirements; and,
- the testing of internal controls and compliance specifically for the following compliance requirements: equipment and real property management, procurement and suspension and debarment, reporting, subrecipient monitoring, and special tests and provisions.

Because the working papers did not contain sufficient documentation to demonstrate compliance with Circular A-133 requirements, we needed significant oral explanations from the auditors. The explanations were needed in order to determine that the audit of internal control over compliance with requirements provided a sound basis for the compliance review and that the extent of testing supported the unqualified opinion on compliance with requirements of the Research and Development program.

GAS requires that the working papers contain enough information about the work performed and the documents examined so that an experienced auditor would be able to examine the same documents and understand the auditor's judgments and conclusions.

As a result of our discussions with the auditors, Grant Thornton prepared supplemental working papers to support the fact that they adequately planned and performed the audit of Federal programs. Based on our review of the supplemental working papers and further discussions with the Grant Thornton auditor, we concluded that the audit generally met Circular A-133 objectives. In addition, Grant Thornton has taken steps to address these deficiencies in future audits through training that will focus on performing procedures to meet Circular A-133 requirements for the audit of internal control over compliance and preparation of working papers that meet GAS documentation requirements.

Reporting Requirements. Grant Thornton did not report all audit findings for Federal awards as required by Circular A-133. Both the Grant Thornton and DCAA audit identified noncompliances with the Allowable Cost/Cost Principles requirement that were not included in the audit report. These issues should have been included in the Schedule of Findings and Questioned Costs and disclosed in the reports on internal control and compliance over major programs. In addition, the audit report on the financial statements did not contain the statement that the audit was conducted in accordance with GAS.

Reporting Audit Findings. Grant Thornton did not report documented findings related to the Allowable Cost/Cost Principles compliance requirement. Grant Thornton and DCAA audits disclosed approximately \$70,000 of questioned costs related to the Allowable Cost/Cost Principles compliance requirement. Circular A-133 requires the auditor to report known or likely questioned costs greater than \$10,000 for a compliance requirement for a major program. The costs questioned were indirect costs, and CTC subsequently removed these costs from its indirect cost rate submission. However, all the costs were questioned as unallowable under several different criteria in OMB Circular A-122, "Cost Principles for Non-Profit Organizations." Grant Thornton stated that they did not report the questioned costs because CTC voluntarily removed them from its indirect cost rate submission.

Circular A-133 requires the auditor to report in the Schedule of Findings and Questioned Costs all reportable conditions in the internal control over major programs and material noncompliances. In addition, known or likely questioned costs greater than \$10,000 for a type of compliance requirement should be reported. Awarding agencies rely on Circular A-133 audit reports to help them monitor and manage their programs. Although CTC corrected the noncompliances by removing the questioned costs from their indirect cost rate submission, Circular A-133 still requires them to be

reported. This information is needed because the Circular A-133 risk-based approach to planning future audits considers several factors including prior audit findings at both the program-level and organization-level for determining the extent of future audit coverage. Failure to disclose these audit findings affects the adequate planning of future audits.

Auditor's Report on the Financial Statements. The Independent Auditor's Report on the financial statements did not contain the statement that the audit was conducted in accordance with GAS as required by Circular A-133. The Standards and American Institute of Certified Public Accountants guidance require that the audit report specifically state that the audit was made according to GAS.

As a result of discussions held with Grant Thornton, they revised the Schedule of Findings and Questioned Costs to include all questioned costs disclosed in the FY 1998 audit and revised the auditor's report on the financial statements to include the required language.

Recommendations

A.1. We recommend that Grant Thornton, LLP, expedite providing the revision of the Office of Management and Budget Circular A-133 audit report to Concurrent Technologies Corporation.

A.2. We recommend that the Executive Director and Treasurer, Concurrent Technologies Corporation, submit a copy of the revised FY 1998 Office of Management and Budget Circular A-133 audit package to the Federal Audit Clearinghouse.

Finding B. Audit Service Costs. CTC charged the Government for unallowable audit costs because it:

- charged Federal awards for \$18,224 of expressly unallowable audit costs related to the potential acquisition of another company, and,
- charged Federal awards for \$48,600 for Grant Thornton's audit of the FY 1998 indirect cost rate submission audit.

Accounting Costs for Acquisition Activity. CTC did not remove expressly unallowable costs for accounting services related to acquisition activity from its FY 1998 certified indirect cost rate submission.

During calendar year 1998, CTC was pursuing the possible acquisition of another company. CTC incurred \$18,224 of costs for audit services provided by Grant Thornton associated with the planned acquisition. These costs are expressly unallowable under Circular A-122 criteria and should not have been included in the CTC FY 1998 certified indirect cost rate submission. DCAA did not question the costs in their audit because the supporting documentation for Grant Thornton's audit service costs did not provide details of the specific services rendered. However, Grant Thornton was also auditing CTC costs for allowability. Grant Thornton should have advised CTC to remove these costs since Grant Thornton was aware of the services performed and should have been knowledgeable about the allowability criteria in Circular A-122.

The Government must be reimbursed for this unallowable cost, and the reimbursement should include assessed penalties and interest as required by Federal Acquisition Regulation 42.709.

We discussed this issue with the CTC Executive Director and Treasurer who agreed that the costs were related to unallowable activity and should have been removed from the CTC certified claim. We were advised that since the CTC FY 1998 indirect cost rates and carryforward amounts have already been finalized, CTC will adjust the FY 2000 indirect cost rate submission to remedy the situation.

Audit of Indirect Cost Rate Submission. CTC paid Grant Thornton \$48,600 to audit their FY 1998 indirect cost rate submission. These audit services were in addition to Grant Thornton's engagement to perform the OMB Circular A-133 audit. These audits were arranged for under separate engagement letters. The Government should not have been charged for the audit of the indirect cost rate submission because:

- the audit was not needed to meet Circular A-133 requirements; and,
- the services contracted for were unnecessary considering the CTC financial internal controls, the absence of prior significant allowable cost issues, and the ability of DCAA to perform this audit as the DoD cognizant contract audit organization.

Circular A-133 requirements. Circular A-133 requires an audit of the financial statements and compliance requirements applicable to major Federal programs. One of the compliance requirements, Allowable Cost/Cost Principles, addresses allowability of direct and indirect costs. The audit procedures performed by Grant Thornton on the allowability of FY 1998 incurred indirect costs were not required due to the nature of the CTC indirect cost rates.

CTC charges the Government for indirect costs using a fixed rate. These rates were negotiated by the Administrative Contracting Officer (ACO) based on a DCAA audit of the proposed rates. Since the basis for the fixed rates for FY 1998 was previously tested, no additional testing of the allowability of costs was needed to fulfill Circular A-133 requirements.

CTC Management of Allowable Costs. Circular A-122 establishes the principles for determining costs of grants, contracts, and other agreements with non-profit organizations. The principles are designed to provide that the Federal Government bears its fair share of allowable costs. One of the factors affecting allowability of cost is that the cost must be reasonable. It is not reasonable for the Government to pay for audit services that duplicate the work performed by the CTC accounting department and that are available at no cost from the DCAA.

CTC is required to prepare and submit a certified submission of its actual indirect cost rates on an annual basis to the Defense Contract Management Agency. The purpose of this submission is for the ACO to establish a carryforward adjustment for the negotiation of fixed indirect rates for future periods. CTC management is responsible for ensuring that unallowable costs are not included in their certified indirect cost rate submission. CTC has policies and procedures that designate responsibility to accounting and procurement personnel for the appropriate treatment of unallowable costs. The cost for the CTC departments to perform this work is recovered from the Federal Government through CTC indirect cost rates. Federal Acquisition Regulation Subpart 42 and DoD Directives direct the ACO to request audits of the indirect cost rate submission from the DCAA. CTC can, of course, contract for audit services to meet its own needs. However, contracting with Grant Thornton to identify unallowable costs in its submission prior to certification, in effect, duplicates the cost of the CTC accounting department and the DCAA audit services requested by the ACO. This cost should not be passed on to the Government.

CTC Comments. CTC does not concur with our position. The Executive Director and Treasurer advised us of the following:

- CTC stated that an oral agreement was reached at a meeting held in 1994. We were advised that both the ACO and DCAA agreed to Grant Thornton's involvement in the incurred cost audit and to the allowability of Grant Thornton's audit costs.
- Grant Thornton's involvement in the incurred cost was an integral aspect of the coordinated audit approach, which represents an efficient approach for the audit organizations and CTC.

- CTC management felt that they needed "the additional comfort" of having Grant Thornton review their indirect cost rate submission before it was certified and submitted to the Government.

Evaluation of CTC Response. We attempted to confirm the oral agreement with both DCAA and the ACO. Neither organization recalled the agreement referenced by CTC. CTC provided us with an agenda and the CTC minutes from the January meeting. However, it appears that the discussion concerning an independent public accounting firm related to the Circular A-133 audit, not to the indirect cost rate submission audit.

Grant Thornton's involvement in the coordinated audit did not require them to be engaged to perform an audit of the indirect cost rates. Grant Thornton planning memos indicate that they performed an audit of incurred costs as part of their financial statement (Circular A-133) audit. This effort was billed and paid for under the single audit engagement.

In addition, it is not reasonable for the Government to pay additional costs for CTC to ensure that its indirect cost rate submission is free from unallowable costs before management certifies it. The Government pays for the screening of unallowable costs by the CTC accounting and procurement personnel through CTC indirect rates and pays for DCAA audit of the indirect cost rate submission as well.

We believe that the coordinated audit process would be enhanced if Inspector General, DoD, auditors were included in CTC audit coordination meetings. Although CTC is responsible for arranging the Circular A-133 audit, the Inspector General, DoD, is responsible for coordinating audit work and reporting responsibilities among auditors to achieve the most cost-effective audit.

Recommendations

B.1. We recommend that the Executive Director and Treasurer, Concurrent Technologies Corporation:

- a. Reimburse the Government for all costs associated with the Grant Thornton audit of the FY 1998 indirect cost rate submission.
- b. Reimburse the Government for all costs related to acquisition activity that was included in its FY 1998 certified indirect cost rate submission including any assessed penalties and interest.

c. Notify the Inspector General, DoD, of future Office of Management and Budget Circular A-133 coordination meetings.

B.2. We recommend that the Defense Contract Management Agency Administrative Contracting Officer cognizant over the negotiation of the Concurrent Technologies Corporation indirect cost rates:

a. Request that Concurrent Technologies Corporation reimburse the Government for the amount of unallowable acquisition costs included in the Concurrent Technologies Corporation FY 1998 certified indirect cost rate submission including penalties and interest as appropriate;

b. Request that Concurrent Technologies Corporation reimburse the Government for all costs associated with the Grant Thornton audit of the Concurrent Technologies Corporation FY 1998 indirect cost rate submission; and,

c. Advise Concurrent Technologies Corporation that the Government will disallow outside accounting firm costs for audits of the Concurrent Technologies Corporation indirect cost rate submission for future years.

Finding C. Circular A-133 Reporting Package. CTC did not submit a complete reporting package as required by Circular A-133. The package did not include a summary schedule of prior audit findings.

Summary Schedule of Prior Audit Findings. The FY 1998 Circular A-133 audit report did not include the required schedule addressing the prior audit finding from the FY 1997 OMB Circular A-133 audit. The FY 1997 audit reported a finding of non-compliance with the Allowable Costs/Cost Principles requirement. The finding, disclosed by DCAA, related to approximately \$40,000 of costs unallowable under OMB Circular A-122 cost principles. Circular A-133 requires the auditee to prepare a summary schedule of prior audit findings as part of the reporting package.

As a result of our review, CTC prepared the required schedule as part of the revised reporting package.

Recommendation

C. We recommend that the Executive Director, Concurrent Technologies Corporation, submit a copy of the revised FY 1998 Office of Management and Budget Circular A-133 audit package, including the Summary Schedule of Prior Audit Findings, to the Federal Audit Clearinghouse.

Other Matters of Concern. CTC engaged Grant Thornton in 1994 using a competitive purchase order. However, in subsequent years, CTC modified the 1994 purchase order without recompeting the procurement. OMB Circular A-110, "Uniform Administrative Requirements for Grants and Agreements With Institutions of Higher Education, Hospitals, and Other Non-Profit Organizations" requires that all procurement transactions be conducted in an open and free competition to the maximum extent practical. In FY 1998, CTC paid Grant Thornton \$440,000 for audit and advisory services. Charges for \$103,600 were related to Circular A-133 (\$55,000) and incurred cost (\$48,600) audits. CTC procured these services without the benefit of competition and without any analysis to determine the reasonableness of the costs. Procurements related to Government audits should be competed in accordance with the standards. CTC does not concur with our position. The Executive Director and Treasurer stated that CTC believes that procurement of Grant Thornton's audit services complied with the procurement standards. However, CTC did not furnish us with any documentation to support their position.

Because this report contains findings and recommendations, written comments are required within 30 days from the date of this report. We appreciate the courtesies extended during the review. If you have questions on this report, please contact Thomas Heacock at (703) 604-8756 (mheacock@dodig.osd.mil) or Janet Stern at (703) 604-8752 (jstern@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 Grant Thornton, LLP, audit of Concurrent Technologies Corporation for the fiscal year ended June 30, 1998, and the resulting reporting submission to the Single Audit Clearinghouse dated November 6, 1998. We performed our review using the 1999 edition of the “Uniform Quality Control Guide for the A-133 Audits” (the Guide). The Guide applies to any single audit that is subject to the requirements of 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 Circular A-133, GAS 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 March 2000 through January 2001 and covered areas related to the financial statements and the one major program, research and development. As the cognizant audit agency for CTC, 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 controls and compliance testing
- Schedule of Expenditures of Federal Awards
- Schedule of Findings and Questioned Costs
- Data Collection Form

In conducting the review, we reviewed all working papers prepared by the auditor, discussed the audit with the auditor and CTC cognizant personnel, and retested selected audit procedures. We also considered the DCAA and Wessel and Co. audits.

Prior Quality Control Reviews

Between January 1996 and January 2000, we performed one quality control review of a Circular A-133 audit performed by Grant Thornton, LLP. We did not identify any findings.

Single Audit Requirements

Circular A-133 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, Circular A-133 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 Circular A-133, 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 in accordance with the OMB Circular A-133;
- Financial statements and related opinion;
- Schedule of Expenditures of Federal Awards and related opinion;
- Report on internal controls 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 a Compliance Supplement (Supplement) annually. The Supplement assists the auditors in determining the audit scope for Circular A-133 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 controls (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
- B.* Allowable Costs/Cost Principles
- C.* Cash Management
- D. Davis-Bacon Act
- E. Eligibility
- F.* Equipment and Real Property Management
- G. Matching, Level of Effort, Earmarking
- H.* Period of Availability of Federal Funds
- I.* Procurement and Suspension and Debarment
- J.* Program Income
- K. Real Property Acquisition/Relocation Assistance
- L.* Reporting
- M. Subrecipient Monitoring
- N.* Special Tests and Provisions

* Compliance requirements applicable to CTC Research and Development program.

Appendix B. Report Distribution

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This report was prepared by the Deputy Assistant Inspector General for Audit Policy and Oversight, Office of the Assistant Inspector General for Auditing, DoD. Personnel of the Office of the Inspector General, DoD, who contributed to the report are listed below.

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