

- ◀ Much of the research supported by NSF in the area of social and economic sciences deals with decision-making under uncertainty—both by individuals and businesses—and applications of game theory. NSF also supports studies in political science, law and social science, sociology, ethics and values, science and technology, archaeology, linguistics, social psychology, and human cognition and perception.

# Independent Auditors' Report and Management's Response

**NATIONAL SCIENCE FOUNDATION**  
4201 WILSON BOULEVARD  
ARLINGTON, VIRGINIA 22230



February 26, 2001

To: Dr. Eamon M. Kelly  
Chairman, National Science Board

Dr. Rita Colwell  
Director, National Science Foundation

From: Christine C. Boesz, Dr. *Christine C. Boesz*  
Inspector General

Subject: Audit of the National Science Foundation's  
Fiscal Years 2000 and 1999 Financial Statements

This memorandum transmits KPMG LLP's report on its Fiscal Years 2000 and 1999 financial statement audit of the National Science Foundation (NSF).

**Results of Independent Audit**

The Chief Financial Officers (CFO) Act of 1990 (P.L. 101-576), as amended, requires NSF's Inspector General or an independent external auditor, as determined by the Inspector General, to audit the Foundation's financial statements. Under a contract monitored by the Office of Inspector General (OIG), KPMG, an independent public accounting firm, performed an audit of NSF's Fiscal Years 2000 and 1999 financial statements. The contract required that the audit be performed in accordance with the Government Auditing Standards issued by the Comptroller General of the United States, and Bulletin 01-02, "Audit Requirements for Federal Financial Statements," issued by the United States Office of Management and Budget.

KPMG issued an unqualified opinion on NSF's financial statements. In their Report on Internal Controls Over Financial Reporting, KPMG did not note any matters that they considered to be a material control weakness. In their Report on Compliance with Laws and Regulations, KPMG identified one instance of reportable noncompliance relating to a potential noncompliance with Federal appropriations law arising from NSF expending funds from its Research and Related Activities appropriation to supplement potential shortfalls in its Major Research Equipment (MRE) appropriation for a large international project. This potential noncompliance with law was identified in a report issued by the NSF OIG in December 2000. NSF management believes, however, that its allocation of costs between the two appropriations was within its discretion under the guiding principles of Federal appropriations law and disagrees with the OIG's assessment. NSF management intends to seek to have language included in future MRE appropriations to clarify that funds from other sources might be used to supplement those in such appropriations.

**Evaluation of KPMG's Audit Performance**

To fulfill our responsibilities under the CFO Act of 1990, as amended, and other related financial management legislation, the Office of Inspector General:

- Reviewed KPMG's approach and planning of the audit;
- Evaluated the qualifications and independence of the auditors;
- Monitored the progress of the audit at key points;
- Examined working papers related to assessing internal controls over NSF's financial reporting process;
- Reviewed KPMG's audit report to ensure compliance with Government Auditing Standards and Office of Management and Budget Bulletin No. 01-02;
- Coordinated issuance of the audit report; and
- Performed other procedures that we deemed necessary.

However, due to the timing for completing the NSF Fiscal Year 2000 Accountability Report, we have not yet completed our review of the working papers prepared by KPMG.

KPMG is responsible for the attached auditor's report dated January 10, 2001, and the conclusions expressed therein. Our review, as differentiated from an audit in accordance with auditing standards generally accepted in the United States of America, was not intended to enable us to express, and accordingly we do not express, an opinion on NSF's financial statements and report on NSF's internal control over financial reporting and compliance with laws and regulations. Nevertheless, we believe that KPMG's work provides a reasonable basis for its report.

The Office of Inspector General appreciates the courtesies and cooperation extended to KPMG LLP and to our audit staff during the audit. If you or your staff have any questions, please contact me or Deborah H. Cureton, Associate Inspector General for Audit.



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## INDEPENDENT AUDITORS' REPORT

Dr. Eamon M. Kelly  
Chairman, National Science Board

Dr. Rita Colwell  
Director, National Science Foundation

We have audited the accompanying balance sheets of the National Science Foundation (NSF) as of September 30, 2000 and 1999, and the related statements of net cost, changes in net position, budgetary resources, and financing (hereinafter collectively referred to as "financial statements") for the years then ended. The objective of our audits was to express an opinion on the fair presentation of these financial statements. In connection with our audits, we also considered NSF's internal control over financial reporting and tested NSF's compliance with certain provisions of applicable laws and regulations that could have a direct and material effect on its financial statements.

### SUMMARY

As stated in our opinion, we conclude that NSF's financial statements as of and for the years ended September 30, 2000 and 1999 are presented fairly, in all material respects, in conformity with accounting principles generally accepted in the United States of America.

Reportable conditions are matters coming to our attention relating to significant deficiencies in the design or operation of internal control over financial reporting that, in our judgment, could adversely affect NSF's ability to record, process, summarize, and report financial data consistent with the assertions by management in the financial statements. Material weaknesses are reportable conditions in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements, in amounts that would be material in relation to the financial statements being audited, may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Because of inherent limitations in any internal control, misstatements due to error or fraud may occur and not be detected. However, we noted no matters involving the internal control and its operation that we considered to be material weaknesses as defined above during the year ended September 30, 2000.

Regarding our consideration of internal control over financial reporting, we identified a reportable condition regarding the reporting of property, plant and equipment during the year ended September 30, 1999. NSF's United States Antarctic Program contractor did not implement internal control policies and procedures to ensure that year-end equipment records provided to NSF were complete. However, we do not believe the property, plant, and equipment



matter was a material weakness. This condition has been corrected during the year ended September 30, 2000.

Regarding our tests of compliance with certain provisions of laws and regulations, we noted one instance of reportable noncompliance with laws and regulations that is required to be reported under *Government Auditing Standards* and Office of Management and Budget (OMB) Bulletin No. 01-02, *Audit Requirements for Federal Financial Statements*, for the year ended September 30, 2000. This instance related to a potential noncompliance with Federal appropriations law arising from NSF expending funds from its Research and Related Activities appropriation to supplement potential shortfalls in its Major Research Equipment appropriation for a large international project. This potential noncompliance with law was identified in a report issued by the NSF Office of Inspector General in December 2000. We noted no instances of reportable noncompliance with laws and regulations related to the year ended September 30, 1999.

Our conclusions and the scope of our work are discussed in more detail below.

## **OPINION ON FINANCIAL STATEMENTS**

In our opinion, the accompanying financial statements present fairly, in all material respects, the financial position of the National Science Foundation as of September 30, 2000 and 1999, and its net costs, changes in net position, budgetary resources, and reconciliation of net costs to budgetary obligations, for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

The information in the *Management's Discussion and Analysis, Required Supplementary Information*, and *Required Supplementary Stewardship Information* sections is not a required part of the financial statements but is supplementary information required by the Federal Accounting Standards Advisory Board and Office of Management and Budget (OMB) Bulletin No. 97-01, *Form and Content of Agency Financial Statements*, as amended. We did not audit the information in the *Management's Discussion and Analysis, Required Supplementary Information*, and *Required Supplementary Stewardship Information* sections, and, accordingly, we express no opinion on it. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of this information. We determined that NSF did not complete the intragovernmental balance reconciliations with its governmental trading partners, as specified by the January 2000 technical amendment to OMB Bulletin No. 97-01, because, although NSF issued confirmations to its major partners, such partners did not respond with adequate information to assist in reconciling balances.

## **INTERNAL CONTROL OVER FINANCIAL REPORTING**

Our consideration of internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be reportable conditions. Under standards issued by the American Institute of Certified Public Accountants and OMB Bulletin 01-02, reportable conditions are matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over financial reporting that, in our

judgment, could adversely affect NSF's ability to record, process, summarize, and report financial data consistent with the assertions by management in the financial statements. Material weaknesses are reportable conditions in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements, in amounts that would be material in relation to the financial statements being audited, may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Because of inherent limitations in any internal control, misstatements due to error or fraud may occur and not be detected. However, we noted no matters involving the internal control and its operation that we considered to be material weaknesses for the years ended September 30, 2000 and 1999 as defined above.

Exhibit 1 presents the status of the 1999 reportable condition.

We noted other matters involving internal control and its operation that we have reported to the management of NSF in a separate letter dated January 10, 2001.

#### **COMPLIANCE WITH LAWS AND REGULATIONS**

The results of our tests of compliance with certain provisions of laws and regulations, which include tests of compliance with Federal Financial Management Improvement Act (FFMIA) Section 803(a) requirements, performed as part of obtaining reasonable assurance about whether the financial statements are free of material misstatement, disclosed one instance of potential noncompliance with laws and regulations that is required to be reported herein under *Government Auditing Standards* and OMB Bulletin No. 01-02. This instance of reportable noncompliance relates to a potential noncompliance with Federal appropriations law arising from NSF expending funds from its Research and Related Activities appropriation to supplement potential shortfalls in its Major Research Equipment appropriation for a large international project. This potential noncompliance with law was identified in a report issued by the NSF Office of Inspector General (OIG) in December 2000.

*NSF Management Response: NSF management believes that its allocation of costs between the two appropriations was within its discretion under the guiding principles of Federal appropriations law and disagrees with the OIG's assessment. NSF management intends to seek to have language included in future Major Research Equipment appropriations to clarify that funds from other sources might be used to supplement those in such appropriations.*

We noted no instances of reportable noncompliance with laws and regulations related to the year ended September 30, 1999.

We noted other matters involving compliance with laws and regulations that we do not consider to be material non-compliance, which have been reported to the management of NSF in a separate letter dated January 10, 2001.

## RESPONSIBILITIES

**Management's Responsibility.** The Chief Financial Officer's (CFO) Act of 1990, as amended, requires federal agencies to report annually to Congress on their financial status and any other information needed to fairly present the agencies' financial position and results of operations. To meet the CFO Act reporting requirements, NSF prepares annual financial statements. Management is responsible for:

- preparing the financial statements in conformity with accounting principles generally accepted in the United States of America, and for preparing the other information contained in the FY 2000 Accountability Report
- establishing and maintaining internal controls over financial reporting
- complying with applicable laws and regulations, including FFMIA

In fulfilling this responsibility, estimates and judgments by management are required to assess the expected benefits and related costs of internal control policies.

**Auditors' Responsibility.** Our responsibility is to express an opinion on the financial statements of NSF as of and for the years ended September 30, 2000 and 1999, based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Bulletin No. 01-02. Those standards and OMB Bulletin No. 01-02 require that we plan and perform the audit to obtain reasonable assurance that the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures relating to the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In planning and performing our audits, we considered NSF's internal control over financial reporting by obtaining an understanding of the design of NSF's internal control, determining whether internal controls had been placed in operation, assessing control risk, and performing tests of controls in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements. We limited our internal control testing to those controls necessary to achieve the objectives of OMB Bulletin No. 01-02 and *Government Auditing Standards*. We did not test all internal controls as defined by the Federal Managers' Financial Integrity Act of 1982. The objective of our audits was not to provide assurance on NSF's internal control. Consequently, we do not provide an opinion on internal control over financial reporting.

In addition, as required by OMB Bulletin No. 01-02, we considered NSF's internal control over *Required Supplementary Stewardship Information* by obtaining an understanding of NSF's

internal control, determining whether these internal controls had been placed in operation, assessing control risk, and performing tests of controls. Our procedures were not designed to provide assurance on internal control over *Required Supplementary Stewardship Information*, and, accordingly, we do not provide an opinion on such controls.

As further required by OMB Bulletin No. 01-02, with respect to internal control related to performance measures determined by management to be key and reported in *Management's Discussion and Analysis* section of the FY 2000 Accountability Report, we obtained an understanding of the design of significant internal controls relating to the existence and completeness assertions. Our procedures were not designed to provide assurance on internal control over reported performance measures, and, accordingly, we do not provide an opinion on such controls.

As part of obtaining reasonable assurance whether the NSF's financial statements are free of material misstatement, we performed tests of NSF's compliance with certain provisions of laws and regulations, noncompliance with which could have a direct and material effect on the determination of the financial statement amounts, and certain provisions of other laws and regulations specified on OMB Bulletin No. 01-02, including certain requirements referred to in FFMIA. We limited our tests of compliance to these provisions, and did not test compliance with all laws and regulations applicable to NSF. However, providing an opinion on compliance with laws and regulations was not an objective of our audit, and, accordingly, we do not express such an opinion.

Under OMB Bulletin No. 01-02 and FFMIA, we are required to perform tests of compliance with FFMIA Section 803(a) requirements, which indicate whether NSF's financial management systems substantially comply with (1) Federal financial management systems requirements, (2) applicable Federal accounting standards, and (3) the United States Government Standard General Ledger at the transaction level. The results of our tests disclosed no instances in which NSF's financial management systems did not substantially comply with these requirements.

#### **DISTRIBUTION**

This report is intended solely for the information and use of NSF's management, the NSF Office of Inspector General, OMB, and Congress, and is not intended to be and should not be used by anyone other than these specified parties.

*KPMG LLP*

January 10, 2001

**Exhibit 1****Status of 1999 Reportable Condition**

**1999 Condition:** NSF's United States Antarctic Program (USAP) contractor did not implement internal control policies and procedures to ensure that year-end equipment records provided to NSF were complete. NSF, through its contractor, maintains research facilities in New Zealand and Antarctica where over 95 percent of NSF's assets reside. We performed extensive interim testing prior to year-end at the contractor's site and found equipment additions properly recorded in the contractor's records. We found, however, that these additions were not recorded at year-end in either the contractor records or NSF's general ledger. We believe that as a result of these conditions, NSF cannot routinely compile complete and accurate property information related to contractor-held equipment additions for financial reporting. As a result of our testwork and recommendations, however, NSF adjusted contractor-held equipment additions to accurately report activity in the financial statements.

**1999 Recommendations:** We recommend that NSF implement procedures to ensure complete and accurate reporting of contractor-held equipment.

**2000 Management's Response:** Procedures were implemented by the USAP Contractor during fiscal year 2000 to reconcile equipment additions recorded and reported during the year to the total additions for the year that had been recorded and reported at year-end to NSF. Additionally, NSF management instituted a supervisory level of review and concurrence with accounting information prepared by contractor staff to identify and correct any errors and improper reporting before information is submitted to NSF.

**2000 KPMG's Assessment:** Corrected