Date: March 29, 2013

To: France Cordova, Chair of the Board of Regents
    John McCarter, Chair of the Audit and Review Committee

cc: G. Wayne Clough, Secretary
    Albert Horvath, Under Secretary for Finance & Administration/Chief Financial Officer
    Andrew Zino, Comptroller

From: Scott S. Dahl
       Inspector General


The Office of the Inspector General (OIG) serves as the Smithsonian’s Contracting Officer’s Technical Representative for the oversight of the Smithsonian’s annual financial statement audits performed by the independent public accounting firm of KPMG LLP (KPMG). KPMG audited the Smithsonian Institution’s fiscal year (FY) 2012 Federal Closing Package (federal appropriations reporting) and the Smithsonian’s FY 2012 entity-wide Financial Statements (combined federal and trust reporting).

This letter summarizes the KPMG audit reports, its Management Letter Comments, and our statement of KPMG’s adherence to auditing standards.

**KPMG’s Financial Audit Reports of the Smithsonian**

KPMG issued the following reports in accordance with contract requirements:

*Special-Purpose Financial Statements* – on November 15, 2012, KPMG issued an unqualified opinion on the FY 2012 federal special-purpose financial statements, also known as the federal closing package.

*Entity-Wide Financial Statements* – on January 31, 2013, KPMG issued an unqualified opinion on the Smithsonian’s FY 2012 entity-wide financial statements. KPMG audited the statement of financial position as of September 30, 2012, and the related statements of financial activity and cash flows for the fiscal year. KPMG concluded these financial statements present fairly, in all material respects, the financial position of the Smithsonian Institution as of September 30, 2012, and its changes in net assets and its cash flows for the fiscal year, in conformity with U.S. generally accepted accounting principles.
Management Letter Comments

KPMG reported no material weaknesses or significant deficiencies in their FY 2012 management letter. However, KPMG made the following observations:

- The Smithsonian had made errors in classifying temporarily restricted net assets correctly.

- The Smithsonian’s controls had not detected or corrected some financial reporting issues. For example, the fixed assets depreciation expense was overstated by $3.1 million; there were inaccurate year-end cutoffs for two federal accounts payable and construction accruals; and the deferred rent liability was understated due to the exclusion of certain leases that should have been included in the schedule of future minimum lease payments that supports this liability.

- Unit-level accounting at the Smithsonian resulted in the application of inconsistent polices in of situations between or among units of the Smithsonian in the areas of private grants and contracts, cash contributions, deferred lease liabilities, exchange transactions, and manual journal entries.

- The Smithsonian could improve information technology controls and reduce significant vulnerability risks by ensuring software is updated promptly and by effectively reviewing network and data center access levels.

- The Smithsonian had not promptly submitted audited financial and certain non-financial data as required by the covenants of its two outstanding debt issues.

Management has taken, or plans to take, corrective actions to address these comments.

KPMG’s Adherence to Audit Standards

In connection with our oversight, we reviewed KPMG’s reports and audit documentation and interviewed its representatives. Our review of KPMG’s FY 2012 audit work disclosed no instances where KPMG did not comply, in all material respects, with the American Institute of Certified Public Accountants’ generally accepted auditing standards and the U.S. Government Accountability Office’s Government Auditing Standards.

Our oversight of KPMG’s audit was not intended to enable us to express, and we do not express, an opinion on the Smithsonian’s financial statements, internal control, or compliance with laws and regulations. KPMG is responsible for their audit reports and the conclusions therein.
If you have any questions, please do not hesitate to call me, or Michael Sinko, Assistant Inspector General for Audits, at 202.633.7050.

Attachment