Audits of Sponsored Research: Introduction

Work actively with researchers and senior management to provide value-added service

By Adrienne Larmett, MBA, Frank Bossle, CPA, and Kimberly Ginn

This is the first of a three-part series on auditing sponsored research, covering the regulatory landscape, risks associated with noncompliance, obstacles to compliance and the role of internal audit. Subsequent articles will address key areas of focus throughout the sponsored research lifecycle.

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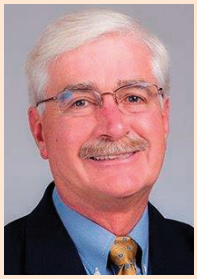

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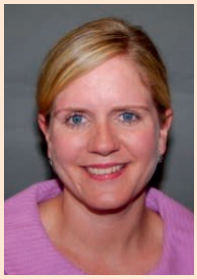

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The federal government provides a majority of the funding that institutions and hospitals receive in support of various types of research. Organizations, as stewards of federal dollars (i.e., taxpayer dollars), are required to comply with myriad regulations governing how sponsored research monies may be expended.

The consequences for noncompliance with federal regulations as well as agency and award terms and conditions can be severe. Therefore, it is essential that organizations develop good oversight and monitoring practices to mitigate the risk of noncompliance. These organizations also need assurance that their system of internal controls is working properly.

Regulatory landscape

There are a number of regulations governing how organizations may spend federal research dollars. The Office of Management and Budget's (OMB) OASC-3, *Principles for Determining Costs Applicable to Research and Development Under Grants and Contracts with Hospitals,* sets forth the requirements. For most other organizations that are recipients of federal extramural funding, the Uniform Guidance applies.

For over 30 years, the cost principles that have been outlined in OMB circulars A-21, A-110, A-122, and A-133 (along with agency and award terms and conditions) provided the guidance to institutions of higher education, nonprofits and foundations on administering and charging research costs to federal awards.

In 2014, to streamline and reduce the administrative burden imposed by the regulations, the eight OMB circulars (A-21, A-50, A-87, A-89, A-102, A-110, A-122 and A-133) were consolidated into a single document: *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards.*

The Uniform Guidance cost principles remain largely consistent with legacy circulars. This means principal investigators (PIs) are still responsible for ensuring their research costs expended against federal awards are actual costs that are allowable, allocable and reasonable. The Uniform Guidance provides the following definitions:

- *Allowable* – A cost is allowable if it is necessary and reasonable for the performance of the federal award (200.403).

- *Allocable* – A cost is allocable to a particular federal award or other cost objective if the goods or services involved are chargeable or assignable to that federal award or cost objective in accordance with relative benefits received (200.405).

- *Reasonable* – A cost is reasonable if, in its nature and amount, it does not exceed that which would be incurred by a prudent person under the circumstances prevailing at the time the decision was made to incur the cost (200.404).

While the Uniform Guidance seemingly became less prescriptive in some areas (e.g., time and effort reporting) it may have created new burden in other areas (e.g., subrecipient monitoring, procurement, internal controls). Although the guidance has been in effect since December 2014, organizations are still figuring out how to address the additional requirements. No one wants to be a first adopter in many of these areas; many are waiting to see how auditors, both external and agency, approach and interpret the new rules.

Noncompliance

Research is replete with risk. Beginning with the proposal phase through the closeout of an award, PIs and organizations alike assume a great deal of risk. The payoff potential is significant, particularly if there is a discovery made or a patentable technology developed.

However, the consequences for noncompliance may be as steep as the potential payoff, and can include fines, penalties and even debarment from future research funding. The misuse of award funds and the subsequent submission of false claims may be considered a violation of the False Claims Act (FCA), which can result in civil penalties for fraudulent claims made to the government.

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Violation of the FCA is subject to damages and mandatory penalties of $5,500 to $11,000 per false claim, which can result in very large penalties. For example, the University of Florida settled a False Claims allegation with the Department of Justice, agreeing to repay nearly $20 million to the government for improperly charging the Department of Health and Human Services for salary and administrative costs on hundreds of federal grants.

Obstacles to compliance

Because the risk associated with noncompliance with regulations can be significant, it is critical to have processes in place for managing and monitoring sponsored research.

Enacting compliant processes is difficult for several reasons:

- *Regulatory language* – Regulations may be hard to interpret and apply.

- *Regulatory application* – Application of regulations may be challenging due to the nature of the research, since no two projects are alike. What may be allowable in one situation may not be allowable in another—it depends.

- *Knowledge deficit* – Experience levels of individuals managing and monitoring awards vary. Managing

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sponsored research may not be a primary responsibility for many administrators. Some organizations may not have dedicated personnel to manage and oversee sponsored research. Therefore, there may be a knowledge/experience deficit.

- *Organizational support* – Organizational resources for sponsored research and guidance may vary. Some may be well developed and centralized, while others may be decentralized, essentially leaving individual departments on their own.

Approaches for success

Internal audit can work with senior leadership to fill the knowledge deficit for sponsored research. Internal audit can serve an essential partner, providing assurance that the monitoring and oversight mechanisms developed and owned by senior leadership are working as intended. Internal audit's role is to serve as a consultative ally, working actively with researchers and providing senior leadership with assurance that monitoring and oversight activities of sponsored research are working properly.

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Internal auditors can assist their organizations by:

1. Assisting researchers and administrators in the interpretation and effective application of regulations
2. Reviewing policies and procedures for consistency with regulations, noting gaps and providing recommendations for achieving consistency
3. Assessing the infrastructure of sponsored research offices, noting process breakdowns, and providing recommendations and best practices to enhance efficiencies and effectiveness of operations
4. Documenting new or existing processes and workflows, as well as evaluating them for effectiveness
5. Performing testing procedures to assess compliance before submitting financial reports
6. Liaising with external agencies
7. Providing input during vendor selection for new systems and technology, and then testing IT controls and assessing staff training after system implementation
8. Educating research personnel about the audit process, particularly the sponsored research audit process

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In their assurance capacity, internal auditors should be careful to emphasize the importance of audit approach, while making the approach meaningful to PIs and administrators. Internal audit must place equal attention to understanding the research administration processes rather than transactions. Transactions may not always reveal the whole story.

For example, a high volume of cost transfers may by itself be cause for concern, but may not disclose the root cause for the high volume. By looking at the entire process, internal auditors may discover inconsistent award management activities at the PI level (e.g., PIs not reviewing their expenses in a timely fashion, resulting in cost transfers).

Additionally, internal auditors should be mindful not to generalize about the population of all award transactions based on a single finding. Audit tools such as data analytics may be helpful for monitoring, but again may not tell the whole story. The why in a process is just as important as the what.

Conclusion

Organizations rely on federal funds to support their research endeavors, and are often willing to accept the corresponding risks in order to achieve their research objectives. Internal audit can serve to mitigate these risks by providing senior leadership with assurance that the monitoring and oversight activities of sponsored research are effective.

The next part in this series will explore issues that arise in the pre-award phase of the award lifecycle and describe how internal audit can serve as an ally in the process. **NP**