

Federal Audit of Grants

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Outline

- **Cost principles**
- **Troublesome expenses**
- **Internal controls**
- **Single Audit**

Part 1: Cost Principles

Cost Principles

- Allocability
- Reasonableness
- Consistency
- Allowability

Allocability: Definition

- The good or service benefits the objectives of the grant.

Allocability: Question 1

A project has \$500,000 of funds to be spent over 3 years. One month to the end of the project, the PI finds out that he still has \$200,000 left, therefore, he decides to buy a piece of equipment for \$160,000 in the last few weeks of the project. Good idea?

Allocability: Question 1

Good idea?

Generally, no. It may be hard to justify how a piece of equipment (or computer) bought in the last days of the project “benefits that project”. If purchased very late, there should be very strong justification.

This is something that auditors can easily detect.

If there are substantial unspent funds AND work to do, please ask for a no-cost extension.

Allocability: Question 2

A PI has two grants, A and B. A technician is working on A and has been so far paid by A. However, grant A funds are almost finished but grant B has lots of remaining funds. Therefore, the PI decides to ask the technician to work on grant A but be paid by grant B. Good idea?

Allocability: Question 2

Good idea?

No. The work of that technician “benefits grant A”, therefore, it is allocable to grant A. If paid by grant B, that is not allocable.

Sometimes because there are not enough funds in one grant, costs are transferred from one grant to the other. **Excessive cost transfers raise the suspicion of costs not being allocable, and they can be easily detected by auditors.**

If errors in assigning costs happen, please try to rectify them quickly. If it takes some time, justifications and plans to repeat such errors are necessary.

Allocability: Question 3

A PI has two grants, A and B. He needs Equipment E, which costs \$30K and will be used for both projects. He estimates that project A uses Equipment E almost twice as much project B. Therefore, he spends \$20K of grant A and \$10K of grant B to buy this piece of equipment. Good idea?

Allocability: Question 3

Good idea?

Yes. This is entirely reasonable. This equipment benefits both projects, therefore, it is allocable to both. Each project pays some of the price, commensurate with use.

Allocability: Question 4

A PI wants to pay her annual dues to the American Association for Cancer Research (AACR) using her National Cancer Institute (NCI) grant. The logic is that being a member of the AACR helps her be a stronger researcher and therefore she can manage this grant better. Good idea?

Allocability: Question 4

Good idea?

Unfortunately, no. The federal government believes that society memberships are useful for the general development of a faculty member, therefore they are **not allocable to a single grant**.

Reasonableness: Definition

- The nature and the dollar amount is what a prudent person would have done under the circumstances.

Reasonableness: Question 1

A PI whose university is located in Baltimore wants to present the results of his findings from Grant A to a large group of people. The largest meeting in his field is usually in Chicago. But he decides to fly to Paris to present the results. He wants to fly first class, as he believes he will have more energy to present when he gets there. He wants to stay in Ritz Carlton, which costs \$3,000 per night. Good idea?

Reasonableness: Question 1

Good idea?

No. These expenses seem to be unreasonable.

The PI may not be able to do this anyway, as **universities typically have some internal controls**. At MSU, such costs are reviewed by the ORA, Office of the Comptroller, and GlobeTrotter.

Please:

- Make sure that the grant allows for international travel.
- Check the per diem and ceiling for hotel expenses.
- Abide by the Fly America Act.

Control Activities at MSU implemented by:

- The Office of Research Administration
- The Office of Procurement
- The Office of Human Resources
- The Office of the Comptroller
- ...

Consistency: Definition

- Like expenses are treated in the same manner under like circumstances.
- In other words, the federal government tells the non-federal entity: “Treat my money as though it is your own.”
- With regards to sponsored projects, this principles manifests itself in at least two ways:
 - Don’t pay using federal funds more than what you pay using MSU funds.
 - Use either “direct” or “indirect” funds but not both.

Consistency: Question 1

A faculty member at MSU receives \$95,000 per year for a 9.5-month contract. She has 2 months of summer funding on her grant, for which she requests \$30,000 of salary. Good idea?

Consistency: Question 1

Good idea?

No. MSU pays this faculty member a salary of \$10,000 per month. Therefore, for two months, she should be paid \$20,000, not \$30,000.

Using federal dollars, we cannot pay a higher rate than we pay at MSU.

Consistency: Question 2

A project receives \$250,000 per year from the NSF. The PI needs an administrative assistant to help him with purchasing, hiring, etc. Therefore, he writes \$30,000 into the grant to pay overtime to an administrative assistant from his department for those questions. Good idea?

Consistency: Question 2

Good idea?

No. This is problematic in at least two ways:

- MSU is charging 26% administrative rate to federal grants as part of its F&A (indirect costs). Therefore, we cannot charge administrative costs in our direct costs again. **This is double-dipping, and against cost accounting standards. This is not consistent spending.**
- If the employee is exempt, payments over 100% institutional base salary using federal funds may be problematic. Extreme care should be taken.

Consistency: Question 2 (continued)

Charging administrative costs as direct costs may be allowed under rare circumstances. It may be allowable when the administrative burden is very large, the employee works full-time and distinct from other jobs for the project, etc.

But, in general, part of the F&A costs need to be redistributed to the units that have the grants, so that they can manage administrative burden of such grants.

Consistency: Question 2 (continued)

In general, the following costs should not be to federal grants:

- Administrative expenses;
- General purpose supplies or equipment (papers, ink, printers, tissues, paper towels).

These purchases can be easily detected by auditors. Only under rare circumstances are they allowable. For example, one can make a case that the paper towels were used for certain experiments.

Allowable: Definition

- Does this particular grant allow for this expense?
- Certain expenses are unallowed at the level of Uniform Guidance (2 CFR 200).
 - More restriction may be imposed by the funding agency.
 - Even more restrictions by the program.
 - And then more restrictions by the State or the University.
- Read the funding opportunity announcement and the notice of award. **Restrictions may be explicitly written or referenced.**

Allowability: Question 1

A PI is applying for a National Institutes of Health (NIH) grant that, if funded, will allow her to spend up to \$100,000 per year in direct costs. She wants to hire a qualified postdoc for her project, because this postdoc can do most of the experiments. She puts this postdoc in her budget and budget justification. Good idea?

Allowability: Question 1

Good idea?

Maybe, or may be not. It depends on whether the funding opportunity announcement allows for hiring postdocs.

Examples:

- NIH R01 grants usually have no restriction on hiring postdocs.
- NIH SCORE 2 grants did not allow for hiring postdocs.

Allowability: Question 2

An MSU PI has a major grant from the National Science Foundation (NSF), with annual direct costs of \$500,000. This PI wants to travel to Paris to present the findings of her study. She procures an economy class flight to Paris via the regular route (MSU / GlobeTrotter) and restricts her per diem and hotel amount to the levels allowed. Good idea?

Allowability: Question 2

Good idea?

Maybe, or may be not. It depends on whether the funding opportunity announcement allows for international travel.

Read the funding opportunity announcement and the notice of award carefully.

Allowability: Question 3

An MSU PI has an institutional base salary (IBS) of \$250,000 per year. In 2022, he spends 20% of his time on this NIH grant and charges 20% of his salary (\$50,000) to this grant. Good idea?

Allowability: Question 3

Good idea?

No. NIH has a salary cap of Executive Level II (congressionally mandated). In 2022, this cap was \$203,700. Therefore, he is only allowed to charge this grant a maximum of \$40,740 ($0.20 \times \$203,700$) for that year.

What happens to the rest of his salary? It should be paid by the institution, which is a form of cost share. (Note: Although this is a form of cost share, it cannot be claimed as cost share, if the grant needs one).

Part 2: Troublesome Expenses / Transactions

Troublesome Expenses / Transactions (1)

- Alcoholic beverages for entertainment
- Other entertainment costs
- Food, especially recurring food
 - Such as for weekly lab meetings
- Substantial budget transfer to travel
- International travel, when not allowed

Troublesome Expenses / Transactions (2)

- Substantial expenditures near the end of the project
- Excessive cost transfers
- Administrative and clerical salaries
- General supplies or equipment

Troublesome Expenses / Transactions (3)

- Paying employees above and beyond institutional base salary
 - Except for rare cases where incidental payment may be allowable.
- Society memberships or dues
- Fines or penalties
- Bad debt write-offs

Troublesome Expenses / Transactions (4)

- Cost overruns
- Rebudgeting to take funds out of participant costs (stipend, tuition)
- Unfulfilled or unaccounted for cost share
- Poor subaward monitoring

Troublesome Expenses / Transactions (5)

- Advertising for the university
- Commencement and convocation costs
- Alumni activities
- Charitable contributions

Part3: Internal Controls

Internal Controls: Definition

A set of processes to ensure:

- Compliance with laws and regulations;
- The integrity of finances;
- Timely, accurate, and reliable reporting.

Internal Controls: Framework

COSO, which stands for the Committee of Sponsoring Organizations of the Treadway Commission, offers one the most widely accepted frameworks.

1. Control Environment
2. Risk Assessment
3. Control Activities
4. Information and Communication
5. Monitoring

Internal Controls

1. Control Environment

- a) Integrity and ethical values at all levels, especially at the leadership level.
- b) Commitment to competence.
- c) Assigning authority and responsibility.

2. Risk Assessment

- a) Process-level objectives.
- b) Risk identification and analysis.

3. Control Activities

- a) Policies and procedures.
- b) Security.

Internal Controls

4. Information and Communication

- a) Quality of information.
- b) Effective communication.

5. Monitoring

- a) Ongoing monitoring.
- b) Separate evaluations.
- c) Reporting deficiencies.

Control Activities at MSU implemented by:

- The Office of Research Administration
- The Office of Procurement
- The Office of Human Resources
- The Office of the Comptroller
- ...

Internal Controls: Question 1

To ensure compliance, University X employs a process in which each expense is reviewed by eight (8) people sequentially. Good idea?

Internal Controls: Question 1

Good idea?

Not necessarily. Control activities and Processes need to be designed carefully.

Too many points of control may be counterproductive.

- Low efficiency
- Higher costs
- Passing responsibility to others
- Going around the rules

Internal Controls: Question 2

University X has a long approval queue. Expenses are approved slowly and inefficiently. Therefore, a PI decides to transfer some of his funds to the University Foundation, so that he can request checks to be cut quickly. Good idea?

Internal Controls: Question 2

Good idea?

Most likely, no.

- Does the Foundation have any internal controls?
- Do they follow procurement rules?
- Do they check if the PI is receiving over 100% effort?

Worst, we may be misleading auditors, when we share our internal controls with them, if some of the funds are not spent under the rule explained to them.

Part 4: Single Audit

Single Audit: What is it?

Each non-federal entity may receive federal assistance (e.g., grants) or cost-reimbursable contracts from many federal agencies. For example, MSU receives funds from the NIH, NSF, DoD, etc.

It is difficult for the non-federal entity to be audited by multiple agencies. Therefore, the federal government accepts a single audit, which has certain specifications.

- Single Audit Act of 1984
- Substantially amended in 1996

Single Audit: To Whom Does it Apply?

Any non-federal entity (NFE) that expends at least \$750K of federal assistance has undergo single audit every year.

It is the responsibility of the non-federal entity to arrange for the audit.

MSU has a single audit; it is a part of the single audit for the State of Maryland agencies. Therefore, our single audit report is part of a larger one.

You may find the audited reports on MSU Comptroller's website.

MORGAN STATE UNIVERSITY
FINANCIAL STATEMENTS AND
SUPPLEMENTARY INFORMATION
YEARS ENDED JUNE 30, 2022 AND 2021



Single Audit: Where Are the Rules?

Uniform Guidance (2 CFR 200)

- Subpart F (Audit Requirements)
- Appendix XI (Compliance Supplement)

2 CFR PART 200, APPENDIX XI

COMPLIANCE SUPPLEMENT



April 2022
EXECUTIVE OFFICE OF THE PRESIDENT
OFFICE OF MANAGEMENT AND BUDGET

Single Audit: Objective and Importance

Objective:

To determine direct and material compliance requirements for each major program

Importance:

- Report card by federal funding agencies and pass through entities
- Tool for federal agencies to address problems at the grantee level or to make broad changes to federal programs
- Assurance to users the compliance of a non-federal entity

Single Audit: The Scope

- Conducted according to GAAS and GAGAS (Detailed in the Yellow Book, issued by the GAO)
- Covers the entire operations of the University
- Financial statements
- Adequacy of internal controls (to minimize fraud and errors)
- Compliance with federal statutes, regulations, and terms and conditions of the award (e.g., Do we comply with the Davis-Bacon Act?)

Single Audit: Auditee Responsibilities (1)

- Arrange for single audit (annually)
- Prepare financial statements
- Prepare the Schedule of Federal Expenditures (SEFA)
- Give the auditors access to all books and records
- Provide summary schedule of previous findings
- Respond quickly to any questions
- Follow-up on audit findings and develop corrective action plans

Single Audit: Auditee Responsibilities (2)

- Disseminate information
- Comply with federal statutes and regulations
- Maintain internal controls over federal programs
 - Various offices at MSU
 - IRB
 - IACUC
 - ...
- Evaluate and monitor compliance
- Take quick action when non-compliance is identified

Single Audit: Auditor Responsibilities (1)

- Audit financial statements in accordance with GAAS and GAGAS
- Determine whether SEFA is presented fairly in relationship to the entire financial statements
- Understand internal controls over major federal programs
- Determine whether the auditee has complied with federal statutes, regulations, and terms and conditions of the award (especially those that have direct and material effects on major programs)
- Conduct compliance testing and transaction tests
- Follow-up on previous findings
- Complete parts of the data collection form (DCF)

Single Audit: The Process (Simplified)

- The auditors start with the SEFA. In other words, they look at the list of all federal award expenditures.
- They categorize awards under “programs and clusters”. In other words, they look into awards that are similar in nature and have similar audit programs.
- They focus more on “larger and higher-risk” programs and clusters.
- If the entity is high-risk, they review a larger percentage of dollar amounts (almost twice). Better never get into trouble.

Single Audit: The Process (More Detailed)

- Start with SEFA.
- Determine programs and clusters.
- Determine Type A and Type B programs.
- Determine low-risk Type A and high-risk Type B programs.
- Type A programs must be audited, unless they are low-risk.
- Type B program may be audited, if they are high-risk.
- The auditors typically audit a certain percentage of awards given to each institution. This percentage is higher for high-risk auditees. For example:
 - 20% for low-risk auditees
 - 40% for high-risk auditees

Single Audit: SEFA

SEFA should be complete.

- List of all federal awards, whether prime or subawards
- Federal agency name
- Passthrough agency name (when applicable)
- Assistance listing (formerly CFDA, e.g., 84.063)
- Cluster name (e.g., SFA or R&D)
- Total for each cluster
- F&A costs

Single Audit: Programs and Clusters

The process is quite elaborate. It starts with the SEFA.

The auditors first determine “federal programs,” primarily based on awards with similar Assistance Listings (AL, previously known as CFDA) numbers. They may also put similar programs together to create “clusters”. Clusters are those programs that are for the same purpose and have similar audit requirements.

SEFA

<i>B</i>	<i>C1</i>	<i>C2</i>	<i>E</i>	<i>I</i>
Assistance Listing #	State Program Title	Program Title	R&D Cluster (Y/N)	Pass-Through Entity Name
10.216	Multi-Institutional Student Experie	1890 Institution Capacity Building Grants	Y	Pass-Through Virginia State University
10.216	Collaborative Efforts to Enhance CI	1890 Institution Capacity Building Grants	Y	Pass-Through Delaware State University
10.310	Geological Agriculture (GeoAg) Appl	Agriculture and Food Research Initiative (AFRI)	Y	
10.310	Evaluation and Optimization of Inno	Agriculture and Food Research Initiative (AFRI)	Y	Pass Through University of Delaware
10.310	Phage Endolysins as Alternative Ant	Agriculture and Food Research Initiative (AFRI)	Y	Pass Through University of Maryland I
11.000	Readiness Assessment of Supplier Di	Readiness Assessment of Supplier Di	Y	Pas Through Texas A&M University
11.303	2016 EDA University Center Economi	2016 EDA University Center Economi	Y	Pass Through University Of Maryland
11.307	HOPE Inside Small Business QOZ coll	Economic Adjustment Assistance	Y	Pass through From Operation Hope
11.307	EDA University Center CARES Supplem	Economic Adjustment Assistance	Y	Pass Through University Of Maryland
11.417	Building Capacity of Land-Based Atl	Sea Grant Support	Y	UMD Center for Environmental Scienc
11.417	Development of Triploid and Tetrapl	Sea Grant Support	Y	UMD Center for Environmental Scienc
11.417	Maryland Aquaculture Extension Spec	Sea Grant Support	Y	UMD Center for Environmental Scienc
11.417	Maryland Sea Grant Research Fellows	Sea Grant Support	Y	UMD Center for Environmental Scienc
11.419	Climate Resilience and Coastal Mana	Coastal Zone Management Administration Awards	Y	
11.472	From Sequence to Consequence: Genom	Unallied Science Program	Y	Pass Through Rutgers University
11.620	NIST Professional Research Experien	Science, Technology, Business and/or Education Outreach	Y	Pass Through Johns Hopkins Universit

Single Audit: Type A and Type B Programs (1)

After determining such programs or clusters, they determine how much funding each program has received and determine Type A and Type B Programs.

Determination of Type A and Type B follows a formula and depends on the amount of institution's total expenditure of federal funds.

For expenditures between \$25M to \$100M, the threshold for Type A vs. Type B is $0.03 \times$ expenditure. For example, if we spend \$80M per year, any program ≥ 2.4 M will be a Type A and anything < 2.4 M will be a Type B program.

Single Audit: Type A and Type B Programs (2)

All Type A programs are audited, **unless** they are considered low-risk.

- Audited in one of the two previous years
- No modified opinion
- No major changes to program directors, etc

- If X number of Type A programs are not audited, because they are low-risk, then at least $0.25 * X$ Type B programs must be audited, primarily chosen from those Type B programs that are higher than 25% of the Type A/B threshold.

- For example, if 10 Type A programs are low-risk, then at least 3 Type B programs will be audited. If Type A/B threshold is \$2.4M, then they will be primarily chosen from Type B programs above \$0.6M.

Items That May Be Reviewed (From Compliance Supplement)

- A. Activities allowed / unallowed
- B. Expenses allowed / unallowed
- C. Cash Management
- D. (Reserved)
- E. Eligibility
- F. Equipment and Real Property Management
- G. Matching, Level of Effort, Earmarking
- H. Period of Performance
- I. Procurement and Suspension and Debarment
- J. Program Income
- K. (Reserved)
- L. Reporting
- M. Subrecipient Monitoring
- N. Special Tests and Provisions

Requirement	A	B	C	E	F	G	H	I	J	L	M	N
	Activities Allowed or Unallowed	Allowable Costs/Cost Principles	Cash Management	Eligibility	Equipment Real Property Management	Matching, Level of Effort, Earmarking	Period of Performance	Procurement Suspension & Debarment	Program Income	Reporting	Subrecipient Monitoring	Special Tests and Provisions
Program Number												
10.000 (no matrix)												
10.500	Y	Y	N	N	N	Y	Y	N	N	Y	Y	N
10.511	Y	Y	Y	N	Y	Y	N	N	N	Y	N	N
10.512	Y	Y	Y	N	Y	Y	N	N	N	Y	N	N
10.514	Y	Y	Y	N	N	N	N	N	N	Y	Y	N
10.515	Y	Y	Y	N	N	N	N	N	N	Y	Y	N
10.516	Y	Y	Y	N	Y	N	N	N	N	Y	Y	N
10.517	Y	Y	Y	N	Y	N	N	N	N	Y	Y	N
10.520	Y	Y	Y	N	Y	N	N	N	N	Y	Y	N
10.521	Y	Y	Y	N	Y	N	N	N	N	Y	Y	N
10.542**	Y	N	N	Y	N	N	N	Y	N	Y	N	N
10.551/10.561 (SNAP Cluster)	Y	Y	N	N	N	Y	N	Y	N	N	Y	Y

Summary from MSU's Most Recent Single Audit

INDEPENDENT AUDITORS' REPORT

Board of Regents
Morgan State University
Baltimore, Maryland

Report on the Audit of the Financial Statements

Opinions

We have audited the accompanying financial statements of the business-type activities and the discretely presented component unit of Morgan State University (the University), a component unit of the State of Maryland, as of and for the years ended June 30, 2022 and 2021, and the related notes to the financial statements, which collectively comprise the University's basic financial statements as listed in the table of contents.

In our opinion, based on our audits and the reports of the other auditor, the financial statements referred to above present fairly, in all material respects, the respective financial position of the business-type activities and the discretely presented component unit of the University, as of June 30, 2022 and 2021, and the respective changes in their financial position and, where applicable, cash flows thereof for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Part 5: Summary

Summary (For the PIs)

- The auditors annually review fiscal transactions, internal controls, and compliance for federal awards (prime awards and subawards).
- Avoid making problematic expenses. Once in trouble, the chances of getting into trouble increases.
- Larger and more complex awards are more likely to be audited. However, smaller grants can always be audited as well. Always do the right thing.
- Be careful about subawards and about cost sharing.

Summary (For the Management)

- Be sure that internal controls are in place. However, there should be a good plan, not just too many signatures.
- Be careful about cost sharing: both fulfilling the promise and accounting properly for it.
- Be sure that the compliance assurances, primarily described in SF-424B and SF-424D, are fulfilled.
- Prepare the SEFA carefully, be responsive to the auditors, and make sure corrective plans are done carefully.