University of Georgia – Athens
Cost Accounting Standards Review

Executive Summary

This executive summary and the following report reflect the results of Jim Vitale & Associates, Inc. focused review of the University of Georgia Research Foundation's Cost Accounting Disclosure Statement (DS-2) reflecting the accounting practices of the University of Georgia at Athens (UGA or the University) as of July 1, 1996 and its accounting practices for FY2002. The goal of this review was to identify changes in accounting practices that must be reported to the Federal government if they vary significantly from the FY1996 submission or practices that may represent a compliance risk for UGA as a Federal grantee. The review made the following determinations:

- Restricted accounts should be exempt from application of Procurement Card process to prevent inappropriate charges to Federal awards. In its place a departmental clearing account could be used to provide streamlined acquisition and appropriate monitoring and control.

- UGA should automate the transfer of budget information from Sponsored Projects to Contracts and Grants Administration to enhance communication and reduce error potential.

- Strengthen charging practices for Dues, Memberships, and Subscriptions on Federal grants and contracts. These type expenditures should be made to an appropriate departmental administration account and not charged as a direct cost to sponsored restricted accounts.

- The University should develop a methodology in the electronic purchasing system to restrict office supply purchases on Federal grants and contracts.

- Departments should be required to assign appropriate object coding for all non-salary expenditures to ensure object code accuracy in compliance with Federal requirements.

- UGA should conduct a sample survey of the Personnel Activity Report System (PARS) process to determine the accuracy of salary charges to Federal awards. As determined, develop additional training on the use and adjustment of the PARS, reconciliation to the Contracts and Grants Administration (CGA) project budgets and periodic monitoring to ensure compliance.

- The University should require the charging of fringe benefits to departmental sales accounts in proration to the salaries charged.

- UGA should establish a maximum period for journal transfers to 90 days after project end date and/or fiscal year. For active, ongoing sponsored restricted accounts establish a policy/procedure requiring transfer of charges within 90 days of discovery. All transfers should require full detailed explanations where the receiving account is a sponsored restricted account.

- The Facilities and Administrative (F&A) Cost Proposal process should screen department administration accounts for non-administrative salaries and non-salary costs.

- UGA should develop a specific process for the development and monitoring of service center rates that result in charges directly or indirectly to Federal research projects. The process should include reflecting the annual budget deficit or surplus in the following rate year calculation as required by Federal regulations.

- Exempt sales accounts from zero balance requirements and develop a process to monitor yearend balances to prevent overcharging on Federal awards.

- During the F&A Cost proposal development process, screen research and instruction accounts as well as Indirect Cost accounts to determine the appropriate functional designation of the account and inclusion in the correct base.

- Implement $5,000 threshold on Federally purchased equipment effective July 1, 2003.

- Prepare an amended Cost Accounting Standards Disclosure Statement and financial impact statement for updates and changes and submit to cognizant Federal agency.

Background

In 1996, the University of Georgia Research Foundation (UGARF) as the recipient of all Federal awards to the University of Georgia submitted to the Federal government a Cost Accounting Standards Disclosure Statement (DS-2 or the Statement). This disclosure statement was prepared in compliance with the Cost Accounting Standards (CAS) implemented January 1995. This document though in the name of UGARF reflects the cost accounting practices, policies and procedures of the University of Georgia (UGA or the University).

The Cost Accounting Standards issued in January 1995 by the Cost Accounting Standards Board were incorporated into the Office of Management and Budget (OMB) Circular A-21 (Cost Principles for Educational Institutions) in 1996 and consists of four specific cost accounting standards.

<u>CAS 501 - Consistency between budgeting and charging</u>

- Requires a university's practices in estimating costs in a contract proposal be consistent with its practices in actual recording and reporting costs
- Requires proposal estimates and subsequent reports be presented in such a manner as to permit comparison of significant cost elements with the actual costs incurred and reported
- Requires the university to follow consistent practices in
    - Classifying costs between direct and indirect cost pools
    - Methods of allocating indirect costs to the contract
- The objective is to facilitate the comparison of the proposal with the actual costs of performing a contract to provide
    - Financial control and accountability
    - Basis for evaluating a university's estimating capabilities

✓ Expenditures included in a proposal budget as a direct cost must be treated as a direct cost for charging to a grant and not treated as an indirect cost.

<u>CAS 502 - Consistency in the identification of direct and indirect costs</u>

- Requires a university to distinguish between those costs it treats as indirect and those it treats as direct
    - All costs incurred for the same purpose, in like circumstances, are either direct costs only or indirect costs only with respect to final cost objectives
- No cost may be treated as direct, if other costs incurred for the same purpose and in like circumstances are included in an indirect cost pool
- No final cost objective may be allocated types of costs that have been treated as a direct cost of any other final cost objective

- Universities required to file must describe
    - The criteria for classifying a type of cost as direct or indirect
    - The circumstance under which a type of cost may be classified as both

✓ A department or unit of the university cannot direct charge grants if the institutional policy is to treat the cost as indirect.

CAS 505 - Treatment of unallowable costs

- Requires any unallowable cost to be identified and excluded from any billing, claim, or proposal applicable to a government contract
- Requires a university to be able to provide evidence that it has
    - Ascertained its unallowable costs
    - Eliminated such costs from proposals and claims
    - Handled such costs appropriately in its cost allocation methodologies
- Requires a university to separate the costs of authorized (contracted) work projects from other work projects whether related to the authorized project or not
- This Standard does not govern the allowability of costs; such is the function of the appropriate procurement or reviewing authority

✓ The University must have a process in place to identify and prevent unallowable costs from being charged to grants.

CAS 506 – Accounting Period

- Requires a university's cost accounting period be its fiscal year unless another period is used as an established practice

✓ The University must use its fiscal year as its accounting period.

An administrative requirement of the CAS process is that the DS-2 on file with the Federal government should reflect the current practices of the reported organization without material or significant variation. A material variation is defined as a change in reported accounting practice that would have a significant impact on the cost of direct and indirect expenditures charged to Federal awards. It is the responsibility of the filing organization, UGA, to file DS-2 amendments as appropriate to report changes in accounting practices. The University is required to include a financial impact statement with the amended DS-2. The amendment is limited to the section or sections that have been altered.

As previously stated, UGA submitted its DS-2 in July 1996 reflecting accounting practices that existed at that time. The Statement as not been reviewed or approved as of this date nor is a review scheduled. The DS-2 review is the responsibility of Department of Health and Human Services (DHHS) Division of Cost Allocation (DCA) and the DHHS Office of Inspector General for Audit (OIG). Due to resource realignment that occurred subsequent to September 11, 2001, DS-2 reviews by the OIG office have been placed on temporary hold.

Despite the review hold, the University is concerned that its accounting practices are consistent with those reported in 1996 and if not, what changes have occurred that need to be reported in an amended Statement. For that reason, UGA retained the services of Jim Vitale & Associates, Inc. (JVA or the Firm) to conduct a limited scope review of UGA DS-2 statement utilizing a focused review approach that would be minimally disruptive to the campus and target areas of special audit interest from peer DS-2 reviews. The goal of the engagement was to provide senior management with a high level assessment of the effectiveness of UGA's written policies and procedures supporting Federally funded research.

The project workplan included:

- Performing a targeted review of high risk areas for Federally Sponsored awards;

- Reviewing specific policies and procedures for effort reporting, cost sharing, travel, service center/recharge operations and indirect cost allocation for compliance with Federal requirements;

- Conducting three consecutive on-site general meetings, focusing on areas directly involved in the support of Federally sponsored research, with campus representatives from:

    - General Administration (Accounting, Pre/PostAward, Property, Space)
    - Academic departments (college/departmental administration)
    - Service/Recharge Centers (Animal care, etc.);

- Preparing final report detailing the results of our vulnerability assessment and identifying high risk practices with recommended action steps; and

- Present report to senior management.

The review results are presented in two sections; (1) references to specific DS-2 sections and (2) other non-DS-2 issues noted during the review.

DS-2 Review Results

Each section has been assigned a "review risk" designation based on prior reviews conducted nationally by DCA and OIG. The levels used are:

- Low – generally not an issue/area of concern due to minimal impact on Federal projects
- Moderate – the issue/area has raised concerns at some institutional reviews so OIG may conduct a limited review of these costs
- High – the issue/area has consistently raised audit and review issues from Federal officials. Potential for violation of cost accounting standards with material impact to Federal awards

Section I – General Information

1.3.0 <u>Treatment of Unallowables Costs</u>
The University as a means to streamline purchases for UGA departments implemented the State's Procurement Card (P-card) process. This "credit card" is linked to an account at the University with a specific individual authorized to make purchases. Because it is a VISA (trademark) card it is available for use at a large number of vendors. The State and University publishes a pamphlet and conducts training on the proper use of the P-card for personnel receiving a card. But, given the growth of internet purchases and purchases outside the local community, there is no effective method for informing all potential vendors.

The P-card's usage creates a DS-2 Section 1.3.0 issue in that UGA's Contracts and Grants office does not review the P-card expenditures prior or subsequent to charging the grants. Purchases on the P-card are automatically charged to the linked account. The responsibility rests with the P-card user to determine if the expense is appropriate or budgeted for on the linked account. The system charge for P-card purchases appears on the account as object of expense number 71490 without detail. For Federal projects, there maybe no budget established for these expenditures until the charges are noticed or project closeout. The P-card charging on Federal awards could result in a 501 violation for inconsistency between budgeting and actual.

Recommendation – Restricted accounts should be ineligible for P-card accounts to prevent inappropriate charges to Federal awards. Utilize a general fund account and then make appropriate transfers if the P-card usage is required. An exception to this approach might be for program project or core awards due to the large activity and the ability to provide more administrative review through grant funded administrative salary support. P-card user and coordinator (designed as department review function) should not be the same individual. An alternative approach could be to link the P-card to a departmental clearing account. Expenditures could then be transferred off to the appropriate account with the detailed object identified according to the type of expense

Review risk: High

Section II – Direct Costs

2.1.0 <u>Criteria for Determining How Costs are Charged to Federally Sponsored Agreement or Similar Cost Objectives</u>
In discussion with the Offices of Sponsored Programs and Contracts and Grants, it was noted that there needs to be an efficient method for the flow of budgetary information between the pre-award and post-award functions. Utilizing a manual process, as is currently employed, can lead to errors in budget identification and financial requirements. Failing to convey strategic budgetary commitments from the award proposal and/or negotiation process could lead to compliance issues during project operations and/or closeout. An example of information vulnerable to miss-communication is cost sharing on grants and contracts. Committed cost sharing represents dollars of support provided by the University on research awards without cost to the Federal government. Committed cost sharing is documented in the actual budget or proposal narrative but it is the responsibility of Contracts and Grants administration to ensure that adequate documentation is maintained for all committed cost sharing. If the University fails to document committed cost sharing, it is a 501 violation concerning an inconsistency between budgeting and actual, as well as a grant compliance issue.

At the start of this fiscal year, Sponsored Programs started keying in cost sharing information to the IMS system so that C&G staff, as well as, departmental administrators who have access to the C&G system can review available system information and identify the amount of cost-share for each specific award. The effectiveness of this process is still being evaluated, but it points to a process whereby, UGA could roll the complete budget being entered by the Sponsored Programs Office to post-award with all other information.

Recommendation – Automate the transfer of budget information from Sponsored Projects to Contracts and Grants Administration to enhance communication and reduce error potential

Review risk – moderate

Memberships, Dues and Subscription costs are normally to be treated as an indirect cost expense. Direct charging these types of expenses are often difficult to justify for the benefit of a single project but have benefits that extend beyond that of a single project's objectives to multiple project and personal benefits. OMB's position is that these costs are to be treated as an indirect cost expense and classified under the Departmental

Administration cost pool. The University has allowed these types of expenses as a direct cost to sponsored restricted accounts which is a practice inconsistent with peer institutions and a CAS 502 violation.

Recommendation: Change the charging practices for Dues, Memberships, and Subscriptions from a direct cost expense to an indirect cost expense. These type charges should be made to an appropriate departmental administration account and not charged as a direct cost to sponsored restricted accounts.

Review risk - high

The University has identified office supplies in its DS-2 as indirect cost expenses and provides training to campus personnel regarding charging office supplies to grants. From our review, departments are still charging office supplies to Federal grants. This is made easier by the electronic purchasing of office supplies used on campus. This is a 502 violation of inconsistent treatment of costs in like circumstances.

Recommendation – Develop a methodology in the electronic purchasing system to restricted office supply purchases on Federal grants and contracts.

Review risk - high

Non-salary expenditures can reach research accounts or indirect cost categories through three methods:

- Paper check requests that are object coded by Expenditure Control
- Electronic requests that are object coded by the department originating the request or
- P-card that is automatically coded 71490

This approach creates a 502 consistency violation that may result in object of expense being inconsistently charged to grant budgets, as well as the charging of unallowable costs.

Recommendation – OMB and other federal agencies look to the Principal Investigator (PI) as the person with the best knowledge of how grant funding is spent. Require departments to assign appropriate object coding for all non-salary expenditures to ensure object code accuracy in compliance with Federal requirements.

Review risk - moderate

2.5.0 Methods for Charging Direct Salaries and Wages

The University utilizes a "Plan Confirmation Methodology" for documenting effort on Federal grants and contracts or F&A components resulting in charges to grants through the F&A process. During our department review, there were significant comments as to the accuracy of the Personnel Activity Report System (PARS). Our review did not disclose any specific instances of errors in the PARS process. But due to the questions raised by academic departments as well as administrative departments, there is a cause for concern. If the PARS process does not reflect the way in which an individual works on a grant then the University could experience a 501 violation (inconsistency between budgeting and actual) as well a compliance exposure on that project.

Recommendation – Conduct a sample survey of the PARS process to determine the accuracy of salary charges to Federal awards. As determined, develop additional training on the use and adjustment of the PARS, reconciliation to the CGA project budgets and periodic monitoring to ensure compliance.

Review risk - high

2.6.1 Method of Charging Direct Fringe Benefits

The University's DS-2 states that "..direct fringe benefits..are specifically identified by individual employee and charged...in such a manner that each paying account pays its prorated share of actual fringe benefits based on the payroll distribution." In practice, departmental sales accounts where salaries are included do not receive an allocation of fringe benefit costs. The applicable amount stays in the general fund account. This appears to be a 502 violation of consistency by sales accounts not receiving their fair share of fringe benefits. This practice is a CAS violation because sales accounts result in charges to Federal awards.

Recommendation – Require the charging of fringe benefits to departmental sales accounts in proration to the salaries charged.

Review risk - moderate

2.8.0 Cost Transfers
The review of this DS-2 item focuses on the indirect cost rate used by the institution for transferring expenditures after the fact (next fiscal year). The premise is it would be a consistency violation to charge the new fiscal period indirect cost rate to the transferred dollars, if the rate had changed. UGA policy is to charge the same rate assessed during the initial charge which is the correct answer.

Based on issues raised by OIG and OMB A-133 auditors, our review determined that the University does not have a policy limiting transfers to a period of 90 days after the fact or fiscal yearend. From our sample of payroll-only transfers in FY2002, after the fact transfers occurred well past 90 days (as much as 1000 days). Of all payroll transfers impacting Federal research projects in FY2002 over thirty percent were over ninety days. This lack of a reasonable cutoff for "after project end" transfers could result in an A-133 finding as well as DS-2.

Recommendation – Establish maximum period for journal transfers to 90 days after project end date and/or fiscal year on Sponsored Restricted Accounts. Transfers on Sponsored Restricted Accounts are to be made within 90 days of the discovery of the error. When charges are being made from one sponsored restricted account to another, a fully documented explanation must detail the rationale of the charge and the reason for all charges being placed on the receiving Sponsored Restricted Account. All transfers to a sponsored restricted account must have appropriate justification prior to transfer.

Review risk - moderate

Section III – Indirect Costs

3.1.0 Indirect Cost Categories-Cost Accumulation
The University provides general fund accounts that are coded Department Administration and are designed to accumulate the departmental support costs for allocation in the F&A process. By definition, this category should include deans, department heads, clerical and other faculty with administrative appointments. Limited review is made of these accounts in the F&A preparation process to determine whose salaries are included in department administrative account. This could represent a potential 502 violation of the consistency standard. Some departments may include unallowable department administration expenditures, specifically non-support salaries or non-administrative faculty salaries, resulting in inconsistent treatment of cost between departments. This component of the University's F&A proposal process was an issue during the last negotiation.

Recommendation – Screen department administration accounts for non-administrative salaries and non-salary costs.

Review risk - low

3.2.0 Service Centers
The University's DS-2 Statement reports that the variance in major service centers are "...monitored closely with no significant variances resulting." Based on our review of animal care and other service center facilities, billing rates are updated infrequently and individual variances are not determined. Rates are established by the appropriate college dean or department head, who are responsible for the budget deficit of the service center. Annual variances resulting from charges for services should be rolled forward into the following year's rate development plan to ensure users are appropriately charged. The

current practice of looking at the total deficit or surplus creates the opportunity for one service to subsidize another which would be a 502 violation for inconsistency.

Departmental sales accounts (recharge centers) charging Federal projects are developed without any review by offices of Sponsored Projects or Contracts and Grants Administration. There is no standardized format (or template) as to the costs that can be included or should be excluded from the rate development. Pricing decisions are limited to the college or department providing the service. The sales accounts are required to be at zero by yearend based on a policy interpretation attributed to the State Budget Director. This limit does apply to state appropriate funds but restricted funds are exempt. The University is currently seeking approval to treat the sales accounts as an exempt group.

Forcing the sales accounts to be at zero by yearend can result in:

- Delayed reporting of income
- Disincentive to control expenditures
- Shifting non service center expenses to the sales account
- Difficulty in budgeting cyclical business operations
- Incentive to abuse subsidy process
- Disincentive to identify full operational costs
  - Exclude salaries and fringe

This treatment of departmental sales accounts creates a potential 502 violation due to the inconsistency of costs and the treatment of deficits and surpluses. Federal awards may be overcharged for services provided by service centers.

Recommendation – Develop a specific process for the development and monitoring of service center rates that result in charges directly or indirectly to Federal research projects. The process should include reflecting the annual budget deficit or surplus in the following rate year calculation. Update Section 3.2.0 item (6) from Y to B subject to the recommended change. Obtain approval to exempt sales accounts from zero balance requirement and develop a process to monitor yearend balances.

Review risk - moderate

3.3.0 Indirect Cost Pools and Allocation Bases

During the F&A proposal development process, state appropriated research accounts and indirect cost accounts are included in the sponsored research base. These accounts are designed to provide the departments with means to accumulate additional research expenditures not charged to grants and contracts. In meeting with representatives from academic departments there seems to be an inconsistency in the treatment of expenditures charged to these State and unrestricted accounts. The accounts represent additional department funding and may be utilized to fund non research activities as the sister accounts for instruction may be funding research activities.

If they represent non-research expenditures their inclusion in the sponsored research base will reduce the University's F&A rate calculation. This is not a CAS violation, but does represent an opportunity to appropriately identify expenditures to the correct base. It could also indicate an overstatement of instruction base by accounts that are identified as instruction but support the research activity, a potential CAS violation. The Controller's office as part of the F&A process conducts some screening of these accounts (primarily the research accounts) to ensure their proper placement in the F&A proposal.

Recommendation – Enhance the screening process for research and instruction accounts as well as IDC accounts to determine the appropriate functional designation of the account and inclusion in the correct base. Continue the screening by object code to identify research type expenses. Recommend that the space survey process be enhanced to accumulate the specific research accounts funding sponsored research space as well as State appropriated and unrestricted funds supporting sponsored research. This process will augment the Controller's office account screening process.

Review risk - low

Section IV – Depreciation and Use Allowances

4.4.0 <u>Criteria for Capitalization</u>
Effective July 1, 2001, the University implemented a new capital threshold for movable equipment of $5,000. The university's rate agreement with the Department of Health and Human Services (DHHS), dated September 30, 2002 authorized the equipment capitalization threshold to increase for Federal awards starting July 1, 2002. This replaced the previous threshold of $1,000 per item. But UGA will not change the equipment threshold for Federally sponsored projects until July 1, 2003 in order to allow adequate time for proposal budget requests to include F&A costs on equipment items costing between $1,000 and $5,000

Recommendation – Implement $5,000 threshold on Federally purchased equipment effective July 1, 2003.

Review risk - low

Section V – Other Costs and Credits

Not reviewed. Outside of focused review scope

Review risk - low

Section VI – Deferred Compensation and Insurance Costs

Not reviewed. Outside of focused review scope

Review risk - low

Section VII – Central System or Group Expenses

Section not prepared by University in DS-2 Disclosure

Review risk – moderate

Federal reviewers and auditors have expressed concerns about the potential for unallowable costs included in central administration costs charged to its university components. These costs are then included in administrative and operations costs allocated to Federal projects through the F&A process.

Non DS-2 Issues Noted in Review

Review of Contracts and Grants Administration files
Use of manila files though low cost creates an opportunity for file data to be presented in a manner that is not conducive to effective and efficient file review. Grant information including modifications, monthly reports and other communications can be misfiled or lost. This practice places a great deal of memory responsibility on the individual CGA staff member responsible for a grant's file. In times of turnover this could be an impediment to grant management.

Recommendation – Increase resources to CGA to enhance and streamline grant recordkeeping and filing methodology.

Departmental Survey Results
Level of understanding and knowledge of OMB A-21 (cost principles for higher education) and CAS (Cost Accounting Standards) is overall low in the departments sampled. Departments rely on CGA to tell them when an item of cost is allowable or unallowable. Departments also rely on CGA for identifying and mentoring costs sharing on Federal projects. During interviews, there was a general desire for additional classes on A-21 cost principles and cost allowability in departments surveyed.

Recommendation - The University should continue to provide and enhance A-21, CAS and other policy and procedural training to departmental officers. This over time will provide the University with a strong base of knowledge to identify issues of compliance and grant administration. Other Universities have had success with implementing mandatory training for new Principal Investigators and Grant recipients. Web-based certification programs have shown significant success with administrators, Principal Investigators, and other Lab personnel responsible for charging Federal grants. UGA should implement mandatory training for personnel working with Federal grants, potentially offering certification upon successful completion of the core training series. Training and certification programs should be ongoing and updated to reflect changes in Federal regulations and agency requirements.

Project Summary
The University needs to strengthen its policies, procedures and training to address the issues outlined in this report. This action requires the development of an amended DS-2 to support the programmatic changes. The amended DS-2 will include a financial impact statement for the amendments reported.