

## MEMORANDUM

**Date:** March 27, 2018

**To:** Steve Relyea  
Executive Vice Chancellor and Chief Financial Officer

**From:** Larry Mandel   
Vice Chancellor and Chief Audit Officer

**Subject:** **Audit Report 17-84, Sponsored Programs – Indirect Cost Recovery, Systemwide**

We have completed an audit of *Sponsored Programs - Indirect Cost Recovery, Systemwide* as part of our 2017 Audit Plan, and the final report is attached for your reference. The audit was conducted in accordance with the Institute of Internal Auditors' *International Standards for the Professional Practice of Internal Auditing*.

I have reviewed the management response and have concluded that it appropriately addresses our recommendations. The management response has been incorporated into the final audit report, which has been posted to the Office of Audit and Advisory Services' website. We will follow-up on the implementation of corrective actions outlined in the response and determine whether additional action is required.

Any observations not included in this report were discussed with your staff at the informal exit conference and may be subject to follow-up.

I wish to express my appreciation for the cooperation extended by the chancellor's office personnel over the course of this review.

c: Timothy P. White, Chancellor



**SPONSORED PROGRAMS –  
INDIRECT COST RECOVERY**

**Systemwide**

Audit Report 17-84  
February 7, 2018

## EXECUTIVE SUMMARY

### OBJECTIVE

The objectives of the audit were to ascertain the effectiveness of operational and administrative controls related to indirect cost recovery for sponsored programs and to ensure compliance with relevant governmental regulations, Trustee policy, Office of the Chancellor directives, and campus and auxiliary organization procedures.

### CONCLUSION

We found the control environment for the areas reviewed to be effective.

Based upon the results of the work performed within the scope of the audit, the operational and administrative controls for sponsored programs indirect cost recovery as of September 14, 2017, taken as a whole, provided reasonable assurance that risks were being managed and objectives were met.

Although the objectives of this audit were met, we observed that some improvements could be made to systemwide policies addressing the proposal approval process, including approvals for indirect cost rate (IDC) exceptions, and on the administration of state awards.

Specific observations, recommendations, and management responses are detailed in the remainder of this report.

## OBSERVATIONS, RECOMMENDATIONS, AND RESPONSES

### 1. POLICIES AND PROCEDURES

#### OBSERVATION

Systemwide policies and procedures relating to certain aspects of the sponsored programs proposal review and approval process needed improvement.

We reviewed policies and procedures relating to proposal and IDC rate approvals for all 23 campuses. In addition, we visited seven campuses to test campus practices relating to the sponsored programs proposal review and approval process.

We found that:

- There were no systemwide policies or procedures addressing the approval process for IDC rate exceptions (IDC rates below the campus federally negotiated rate). Four of the 23 campuses did not have policies or procedures to address campus processes to approve IDC rate exceptions. In addition, in our campus reviews, we noted exceptions related to documented approvals for IDC rate exceptions at two campuses.
- Campuses did not always follow systemwide guidance relating to state awards. *CSU Implementation Guidance on the Assembly Bill (AB) 20/State of California Model Agreement* (Guidance) requires campuses to use the AB20 model agreement for research, training, and public service awards from state agencies issued after January 1, 2016. The Guidance further requires campuses to obtain Office of the Chancellor (CO) approval for any sponsored projects received from a state agency with an IDC rate lower than 25 percent. However, during our review, we noted that only two of the 23 campuses addressed systemwide requirements for state awards in their policies and procedures. Additionally, in our campus reviews, we noted exceptions relating to the use of the model agreement and the failure to obtain the CO's approval for IDC rates lower than 25 percent at three campuses.
- Systemwide policies and procedures relating to the proposal approval process needed clarification. In our campus reviews, we found issues with the delegations of authority for proposal approval at three campuses and issues with appropriate documentation of proposal approval at four campuses. This was in part due to the fact that it was unclear in systemwide policy whether the president and chief financial officer could designate one individual for both the technical and financial review of the proposal, and whether proposals needed to be approved both at the time of submission and prior to acceptance of the award.

Clear and current systemwide policies and procedures improve compliance with state regulations and California State University (CSU) requirements.

**RECOMMENDATION**

We recommend that the CO:

- a. Develop and implement systemwide policies and procedures related to IDC rate approval, incorporating current systemwide guidance relating to state awards.
- b. Review and update existing policies and procedures related to the proposal approval process to clarify the issues noted above.

**MANAGEMENT RESPONSE**

We concur. The CO will:

- a. Develop and implement systemwide policies and procedures related to IDC rate approval, incorporating current systemwide guidance relating to state awards.
- b. Review and update existing policies and procedures related to the proposal approval process to clarify the issues noted above.

This recommendation will be implemented by July 2018.

## GENERAL INFORMATION

### BACKGROUND

Sponsored programs include all work performed under grants or contracts funded by external sources, such as federal agencies, state agencies, and non-profit organizations.

Sponsored program costs are classified as either direct or indirect costs. Direct costs are those that can be specifically identified with a particular sponsored project, or that can be directly assigned to a sponsored project with a high degree of accuracy. Examples include compensation for employees who work on a specific project, or the cost of materials and equipment incurred for a project. Indirect costs, also known as facilities and administrative (F&A) costs, are those that cannot be specifically identified with a particular sponsored project. Examples include depreciation, general operating and maintenance expenses, and compensation for administrators or clerical staff.

All CSU campuses and the CO have a federally negotiated F&A rate with the Department of Health and Human Services (DHHS), which is generally applicable to all federal programs, with some exceptions. This rate is applied to a modified total direct cost base to calculate the total indirect costs to be paid by the sponsor on each project. F&A rates for on-campus research in fiscal year (FY) 2015/16, excluding research at the CO, ranged from 38.5 percent to 54.5 percent. However, data collected by systemwide management on the total indirect costs recovered by campuses for sponsored projects in FY 2015/16 indicates that the average effective F&A rate across all campuses was only 13.8 percent. There are various factors that affect the actual F&A cost amount that campuses are able to recover, such as caps on indirect cost rates for certain federal programs like training grants, and state and non-profit sponsors that set their own F&A cost-rate limits.

There are generally two main components of sponsored program administration: pre-award, which includes activities such as proposal development, review, and submission prior to acceptance of funds; and post-award, which includes administration of a sponsored program after the grant or contract has been awarded. Any deviations from the federally negotiated F&A rate are approved in the pre-award proposal submission process.

Within the CSU, the CO Office of Research Initiatives and Partnerships contributes systemwide support and promotion for CSU research, scholarship, and creative activities and collaborates with the campus grants, research, and sponsored program offices. The CO Sponsored Programs Administration department provides systemwide support related to the administration of research and sponsored programs, including developing systemwide policies, providing training, analyzing legislation, and providing general guidance to campuses and auxiliaries engaged in externally funded projects.

### SCOPE

We reviewed campus policies and procedures for approving exceptions to the federally negotiated F&A rate on sponsored projects for all 23 campuses. We also visited seven campuses: Bakersfield, Chico, Dominguez Hills, Long Beach, Los Angeles, Pomona, and San Bernardino. We interviewed campus personnel and audited procedures in effect from

June 19, 2017, through September 14, 2017. Our audit and evaluation included the audit tests we considered necessary in determining whether administrative and operational controls are in place and operative.

Specifically, we performed a limited-scope review at each of the seven campuses that we visited to test the administration of the proposal and indirect-cost-rate approval process, including clear lines of organizational authority and responsibility, and current and comprehensive policies and procedures. We have provided campus management at each of the seven campuses we reviewed with an informational memo containing the results of our review so that the campuses can take necessary actions as appropriate.

As a result of changing conditions and the degree of compliance with procedures, the effectiveness of controls changes over time. Specific limitations that may hinder the effectiveness of an otherwise adequate system of controls include, but are not limited to, resource constraints, faulty judgments, unintentional errors, circumvention by collusion, and management overrides. Establishing controls that would prevent all these limitations would not be cost-effective; moreover, an audit may not always detect these limitations.

Our testing and methodology, which was designed to provide a review of key administrative, and operational controls, included interviews, walkthroughs, and detailed testing of the indirect-cost-rate approval process. Our review did not include other aspects of management of sponsored program activities.

## CRITERIA

Our audit was based upon standards as set forth in federal and state regulations and guidance; CSU Board of Trustee policies; Office of the Chancellor policies, letters, and directives; campus procedures; and other sound administrative practices. This audit was conducted in conformance with the Institute of Internal Auditors' *International Standards for the Professional Practice of Internal Auditing*.

This review emphasized, but was not limited to, compliance with:

- Code of Federal Regulations Title 2, Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards*
- Integrated California State University Administrative Manual §11002.01, *General Policy Requirements for the Administration of Grants and Contracts in Support of Externally Funded Research and Sponsored Program Activities*
- Government Code §13402 and §13403

## AUDIT TEAM

Senior Director: Michael Caldera  
Senior Audit Manager: Wendee Shinsato  
Senior Auditor: Christina Chen