

Indirect Costs Reimbursement for Research

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GAO-10-937

Presentation Overview

- Background on GAO
- GAO review results
 - *University Research: Policies for the Reimbursement of Indirect Costs Need to be Updated* (GAO-10-937) (Washington, D.C.: September 8, 2010)
 - Recommendation follow-up
- Discussion

About GAO

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 - Integrity - take a professional, objective, fact-based, nonpartisan, nonideological, fair, and balanced approach
 - Reliability - produce high-quality reports, testimony, and other products and services that are timely, accurate, useful, clear, and candid
- Our Work
 - Done at the request of congressional committees or subcommittees
 - Mandated by public laws or committee reports
 - Done under the authority of the Comptroller General

About GAO

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- The agency is headed by the Comptroller General, who is appointed to a 15-year term. The long tenure of the Comptroller General gives GAO a continuity of leadership that is rare within government.
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 - Our diverse staff includes economists, social scientists, accountants, lawyers, and other professionals and specialists in fields ranging from foreign policy to health care.
- Broad authority to investigate how the federal government spends taxpayer dollars.
- Authorized to make recommendations for greater economy or efficiency in public expenditure.

About GAO

- Location: Headquarters in Washington, D.C. and staff in 11 field offices
- Acquisition and Sourcing Management team is one of 13 mission teams

Why Did GAO Review Indirect Costs Reimbursement for Research in 2010?

- The House Committee on Armed Services Report for the Duncan Hunter National Defense Authorization Act for Fiscal Year 2009 mandated GAO's review of DOD's reimbursement of the indirect costs of research.
- GAO had not conducted extensive review of the topic since the early 1990s.

Review Objectives

For higher education institutions performing basic research for DOD, GAO examined:

1. the variation in proposed and negotiated indirect cost rates and factors that may contribute to variations,
2. how and to what extent the administrative cap and the DOD basic research cap limit the government's reimbursement of indirect costs, and
3. the methods DOD uses for overseeing compliance with indirect cost reimbursement for grants, and the extent to which each method was used.

Methodology

To address objectives 1 & 2 we:

- Reviewed the guidance and policies relating to university indirect cost rate-setting and federal reimbursement of indirect costs, such as OMB Circulars A-21 & A-133.
- Interviewed officials at Defense, Health and Human Services, Office of Management and Budget, Education, and the National Science Foundation; also interviewed university officials and their representatives, as well as independent public accounting firms.
- Surveyed a random sample of schools.

Methodology

For the survey we:

- Surveyed a random sample of 178 schools that was generalizable to schools DOD reported as receiving more than \$100,000 in fiscal year 2007 DOD basic research funding.
- Our analysis of the survey focused on schools submitting standard form rate proposals.

Methodology

To address objective 3 we:

- Interviewed independent public accounting firms for the 32 largest university providers of DOD research and collected data on the research component of their university single audits.
- Interviewed DOD grant closeout officials and cognizant audit agency officials.

Objective 1: Variations in Rates

- We found multiple types of variation in indirect cost rates, including:
 - The proposed and negotiated indirect cost rates varied widely from one school to another.
 - The difference between proposed and negotiated rates varied based on cognizant rate setting agency.
 - Proposed and negotiated rates varied based on whether a school received utility cost adjustment.

Objective 2: Impact of Caps

- We found
 - OMB enacted the administrative cap in 1991 with the intent of limiting federal reimbursement for schools' indirect costs.
 - 83 percent of schools proposed administrative costs that were higher than the 26 percent administrative cap.
 - The DOD basic research cap functioned differently than the rate setting and reimbursement structure familiar to schools.
 - 22 percent of schools negotiated a fiscal year 2008 indirect cost rate high enough to be potentially limited by the 35 percent cap on OOD basic research awards.

Objective 3: Use of DOD Oversight Methods

- We found
 - DOD identified three indirect cost oversight methods: the annual single audit, the award closeout process, and agency audits.
 - GAO identified weaknesses in each of these three methods.
 - 4 of the 32 schools GAO examined were not subject to any of the three methods of oversight in fiscal year 2008. The 32 schools are those schools receiving the most DOD basic research funding.

Recommendations

- Based on the work related to variation of rates we recommended that OMB:
 - Identify methods to ensure that the rate-setting process is applied consistently at all schools, regardless of which agency has rate cognizance.
 - Clarify the roles and responsibilities of federal agencies (including DOD, HHS, and OMB) in accepting applications and reevaluating the eligibility of schools to receive the utility cost adjustment.
- Based on our work related to caps we recommended that OMB:
 - Reexamine and determine whether reimbursing administrative costs at a maximum rate of 26 percent achieves the appropriate level of cost control and achieves the government's objective that the federal government bears its fair share of total costs.

Recommendations

- Based on DOD's oversight methods we recommended that DOD:
 - Establish a process for administrative grants/contracting officers to verify at grant closeout whether a school has requested reimbursement at the accurate indirect cost rate and dollar amount.
 - Assess the current level of audit coverage for monitoring DOD indirect cost reimbursement and determine what level is sufficient and whether to expand use of closeout audits and other audits to oversee compliance.
 - Develop a policy for oversight of indirect costs that includes the use of alternative oversight information (1) for those schools not individually audited under the single audit, and (2) for those schools where the audit coverage of research and development awards is not sufficient for oversight of indirect costs.

Recommendation Follow-up

- GAO follows up annually with agencies to determine the extent to which report recommendations have been implemented.
- Recommendations are either:
 - Closed, implemented
 - Closed, not implemented
 - Open
- Status of GAO report recommendations is publicly available on GAO website: www.gao.gov/products/GAO-10-337/#recommendations

Current Recommendation Status

Agency	Description	Status
OMB	Consistent application of rate setting process.	Open
OMB	Utility cost adjustment	Open
OMB	Administrative cap	Open
DOD	Verifying accurate indirect cost reimbursement.	Closed, implemented
DOD	Assess level of audit coverage	Open
DOD	Policy for use of alternative oversight information	Open

GAO's Related Work

- *Federal Grants: Improvements Needed in Oversight and Accountability Processes* (GAO-11-773T) (Washington, D.C.: June 23, 2011)

GAO Team

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- Support from team members in Denver and other experts within GAO (e.g., statisticians, methodologists, accountants, lawyers, economists)

UNIVERSITY RESEARCH

Policies for the Reimbursement of Indirect Costs Need to be Updated

Why GAO Did This Study

In fiscal year 2007, the majority of the Department of Defense's (DOD) basic research obligations were provided to higher education institutions. DOD reimburses these institutions for both direct and indirect costs for research. Two federal agencies, DOD and the Department of Health and Human Services (HHS), negotiate indirect cost rates used to reimburse higher education institutions for indirect costs on federally funded research awards, including DOD awards.

GAO was asked to examine the following issues related to higher education institutions performing basic research for DOD: (1) the variation in proposed and negotiated indirect cost rates and factors that may contribute to variations; (2) how and to what extent the administrative cap and the DOD basic research cap limit reimbursement of indirect costs; and (3) the methods DOD uses for overseeing compliance with indirect cost reimbursement for grants. GAO surveyed a generalizable sample of higher education institutions performing basic research for DOD, reviewed agency guidance and policies; and interviewed officials from federal agencies, independent public accounting firms, and higher education institutions.

What GAO Recommends

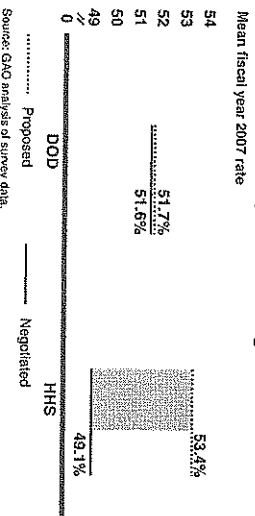
GAO is making recommendations to address consistency in rate-setting and to improve oversight of indirect cost reimbursement. The agencies generally agreed with these recommendations.

View GAO-10-937 or key components. For more information, contact John Needham at (202) 512-4841 or NeedhamJ1@gao.gov.

What GAO Found

GAO identified wide variation in indirect cost rates at schools receiving DOD funding in fiscal year 2007, which may be related to a number of factors. For example, the average difference between a school's proposed and its negotiated rate was much larger for schools with HHS as the cognizant rate-setting agency than for those with DOD (see figure below), in part due to the agencies' differing approaches to negotiation. GAO also found that schools receiving a 1.3 percent add-on to their rate to assist with the cost of utilities both proposed and negotiated higher rates than those without the adjustment. Contrary to guidance to periodically review school eligibility, the fixed list of schools eligible to receive this add-on has not been revisited since established in 1998.

Estimated Mean Proposed and Negotiated Rates at the Two Cognizant Rate-Setting Agencies



Source: GAO analysis of survey data.

The cap on the administrative portion of the indirect cost rate limited fiscal year 2007 reimbursement for about 83 percent of schools. The cap was established nearly 20 years ago with the intent of limiting federal reimbursement for schools' administrative costs, and OMB has not reexamined this cap since its implementation. We estimate the DOD basic research cap might have limited fiscal year 2008 reimbursement for some awards at about 22 percent of schools, but the limitation depends on the types of costs included in each individual award and is difficult to determine up front on a schoolwide basis until total costs for each award are tallied.

GAO identified weaknesses in the three methods DOD says it uses to oversee that indirect costs for research grants are reimbursed appropriately: the single audit, the closeout process, and audits by DOD's Defense Contract Audit Agency or by cognizant agencies for audit. At least one of the three methods was used at most of the schools we reviewed, but four schools were not covered by any of the methods, indicating a gap in coverage. In our discussions with cognizant agencies for audit, we learned that recent audits of research awards to schools at HHS have led to some significant findings of improper billings of indirect costs. Inconsistencies in rate-setting and reimbursement processes lead to perceived and actual differences in the treatment of schools. Moreover, because of the weaknesses in its oversight methods, DOD lacks assurance that it is reimbursing indirect costs appropriately.

