

# Research Audits

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## I. Introduction

Audits are a regular part of the administrative process at NM Tech. External audits are reviewed by and coordinated with the V.P. Administration and Finance and Director of Finance.

The Single Audit Act and OMB Circular A-133 require a coordinated approach between all audit organizations that audit a university. A coordinated approach in the audits of educational institutions results in economies gained through mutual reliance and avoids duplication of effort on various tests and procedures.

## II. Purpose

The purpose of a cost audit (direct or indirect charges) is to determine the following four factors

**A) Allowability** – *for reimbursement purposes pertains to direct and indirect charges* determined by the terms of the governing sponsored agreement or by cost principles established by the federal government in OMB Circular A-21. For example, A-21 specifically defines certain types of expenses e.g., alcohol, lobbying or entertainment as unallowable. Other costs may be unallowable per the specific terms of an award e.g., unapproved foreign travel or equipment costs. These type of expenses are therefore, by definition, unallowable. Auditors are always alert to the possibility that unallowable costs might have been charged. Therefore, they may devote considerable energy to testing specific transactions to see if they fall into an unallowable category.

Note: A cost which is unallowable for a sponsored project may be an appropriate expense for NM Tech. For example, alumni activities is a very appropriate NM Tech activity. Alumni expenses, however, are unallowable for overhead reimbursement purposes, i.e., they may not be charged to the government indirectly.

**B) Allocability** – a cost is allocable to a particular cost objective (i.e., a specific function project, sponsored agreement, department or the like) if the goods or services involved are chargeable or assignable to such cost objective in accordance with relative benefits received or other equitable relationship. Allocability is not the same as allowability; an otherwise allowable cost, e.g., salary or travel may be unallocable to a particular account if the project supported by that account did not benefit from the costs.

**C) Reasonableness** – a cost may be considered reasonable if the nature of the goods or services acquired or applied, and the amount involved therefor, reflect the action that a "prudent person" would have taken under the circumstances prevailing at the time the decision to incur the cost was made.

An auditor may legitimately question a cost that is clearly allocable and not otherwise unallowable if, in the auditor's judgment, the cost exceeds what a reasonable person would have paid in similar circumstances.

**D) Consistently treated** - like expenses must be treated the same in like circumstances.

**Auditors question, but do not disallow costs.** If auditors identify financial transactions that they believe to be inappropriately classified, unreasonable, unallocable, or unallowable, they will question that transaction. Final decisions about the ultimate allowability of a questioned cost are made by a cognizant contracting official taking into account the auditor's report and NM Tech's response.

### **III. Types of Audits**

#### **A) Property Control Audit**

Property Control Systems Analysis (PCSA) audit the purpose of which is to ascertain if NM Tech's property control system is satisfactory to provide control, protection, preservation and maintenance of all Government property; and otherwise within the requirements of the Federal Acquisition regulations (FAR 45.5), Defense Supplement to the FAR (DFAR 245.5), OMB Circulars, **and other applicable agency and contractual requirements.**

#### **B) Preaward Audits**

Preaward audits are typically conducted by DCAA and other sponsor auditors to verify the estimated costs submitted in proposals for large sponsored research projects. Audits may be desk or on-site. Involves proposal preparation staff and/or Principal Investigators. May also involve human resources, purchasing, and fiscal personnel. Preparation normally entails accumulating cost documentation for all proposed direct costs.

#### **C) Claimed Cost Audits**

Sponsors may request their auditors to verify the allowability, allocability, and reasonableness of direct costs that have been charged and billed by NM Tech, especially in connection with cost-reimbursable grants and contracts. Audits of claimed direct costs are most commonly carried out at the completion of the sponsored project, when NM Tech has presented a final invoice to the sponsor.

#### **D) Indirect Cost Audits**

NM Tech recovers its Facilities and Administration costs ( F&A and also known as indirect costs) associated with sponsored projects through the application of indirect cost rates to sponsored project billings. F&A costs represent a recovery of actual expenses incurred in support of sponsored research paid generally from State of NM funds.

NM Tech annually prepares a proposal and incurred cost study to serve as the basis for negotiating a rate with the Office of Naval Research (ONR). DCAA (Defense Contract Audit Agency) audits these proposals and cost studies to advise ONR on the allowability, allocability, and reasonableness of proposed and incurred indirect costs.

#### **E) Compliance and General Control Audits**

Educational institutions are required to comply with a large and constantly changing array of government rules and regulations. Auditors of all types depend on NM Tech's internal controls to achieve compliance, and they periodically undertake separate audits to test the effectiveness of those controls. Our independent public accountants annually conduct a single federal compliance audit as required by the provisions of OMB A-133: Audits of States, Local Governments and Non-Profit Organizations.

#### **F) Financial Statement Audits**

Annually, the independent public accountants for NM Tech conduct audits to assess the accuracy and fairness of the University's year-end financial statements.