

**COVERAGE OF INDEPENDENT AUDITS FOR OTHER
TRANSACTIONS (10 CFR 603)**

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PART 1. GENERAL INFORMATION

What is the purpose of this document?

This document provides guidance for an independent public accountant (IPA) who is asked by a for-profit firm to conduct an audit of its systems, due to the firm's having received a technology investment agreement (TIA) from the Department of Energy (DOE).

Why does the Federal Government need an audit?

Federal officials are accountable to the public for the resources provided to carry out Government programs. Financial auditing contributes to accountability by providing an independent assessment to assure that recipients are handling Government funds properly.

Can the audit be integrated with the regular audit of a firm's financial statements?

Yes, the intent is to cause the minimum possible disruption to the firm's activities, so the IPA is encouraged to do the needed transaction sampling for DOE awards as part of the regularly scheduled audit of the firm's financial statements. In some cases, it may

be even more efficient and economical to separately audit the individual DOE awards, and the firm may elect to have the IPA do so.

What are the objectives of the audit?

The auditor is to determine and report on whether:

- The firm has an internal control structure that provides reasonable assurance that it is managing DOE awards in compliance with the award terms and conditions, including applicable Federal laws and regulations.
- Based on a sampling of DOE award expenditures, the firm has complied with award terms and conditions, including applicable Federal laws and regulations, that may have a direct and material effect on DOE awards.

What is the source of the requirement for the audit?

The source of the requirement stated in the award document stems from sections 603.640 through 603.660 of 10 CFR part 603.

What should the IPA do if he or she finds that the Defense Contract Audit Agency is performing audits of the firm?

The IPA should consult with officials of the firm to ensure that:

- DOE contracting officer was aware of the DCAA audit presence at the time they made awards; and
- The DOE agreement authorizes the IPA to perform the audit, rather than requiring that the DCAA do so. If the IPA is authorized to perform the audit, he or she must consider the nature, timing, and extent of his or her own auditing procedures, to avoid unnecessary duplication of the DCAA effort.

PART 2. AUDIT OBJECTIVES AND COMPLIANCE REQUIREMENTS

A. ALLOWABLE COSTS

What is the objective of this portion of the audit?

The objective is to determine, by testing a sample of transactions, whether the firm complied with the requirements concerning allowability of costs charged to DOE awards.

What standards or cost principles determine the costs that are allowable as charges to the award?

Each technology investment agreement should specify the standards or cost principles that the for-profit firm is to use to determine the costs that it is allowed to charge to that award. While the TIA may specify use of the for-profit cost principles in the Federal Acquisition Regulation (FAR, at 48 CFR part 31), it could specify an alternative standard. The minimum standard in the latter case is that Federal funds and the firm's cost sharing contributions will be used only for costs that a reasonable and prudent person would incur in carrying out the RD&D project contemplated by the agreement.

What compliance requirements for allowability of costs should the audit address?

For a firm that is subject to the cost principles in the FAR, the IPA should determine and report on whether costs charged to DOE awards are in compliance with those cost principles and indirect cost rates are applied in accordance with approved rate agreements.

For a firm that is subject to alternative standards that may be used for a TIA, the IPA should determine and report on whether costs charged to the DOE awards are:

- Necessary and reasonable for the performance of the RD&D projects supported by the awards, or for related administration. Generally, elements of cost that appropriately are charged are those identified with RD&D and development activities under the Generally Accepted Accounting Principles (see Statement of Financial Accounting Standards Number 2, "Accounting for RD&D and Development Costs," October 1974).

- Allocable to the RD&D projects (i.e., costs are charged to DOE projects in a manner that is in accordance with the benefits the projects received).
- Given consistent treatment with costs allocated to the firm's other RD&D and development activities (e.g., activities supported by the firm itself or by non-Federal sponsors).
- In conformance with any limitations in the award documents or regulations that they cite (e.g., any restrictions on types or amounts of costs, or requirements for prior approval of DOE contracting officer).
- Supported by appropriate documentation in the firm's records. The documentation may be in electronic form.

B. COST SHARING

What is the objective of this portion of the audit?

The objective is to determine, by testing a sample of cost sharing contributions, whether the firm made the contributions that the agreements required.

What are the compliance requirements for cost sharing?

The provisions of the award documents will specify requirements for the firm's cost sharing, which may be contributions of a specified amount or a percentage of total project costs. The cost sharing may be in the form of allowable costs incurred or in-kind contributions (including third-party in-kind contributions).

The values of the firm's contributions are determined in accordance with sections 603.530 through 603.555 of 10 CFR part 603.

C. FINANCIAL REPORTING

What are the objectives of this portion of the audit?

The primary objective is to determine whether the firm's financial reports for DOE awards:

- Fairly and completely represent the expenditures and

status of resources for projects supported by those awards; and

- Are supported by applicable accounting records and the accounting basis used (e.g., cash or accrual).

What are the compliance requirements for financial reporting?

The agreements will specify the frequency and content of business/financial reports. They may specify the use of standard financial forms or periodic reports that include information on both programmatic and business status.

Each financial report (and the business portion of any report that also has programmatic information) will contain at least summarized details on the status of resources (Federal funds and any non-Federal cost sharing that the agreements require), including an accounting of expenditures for the period covered by the report. The report should compare the resource status with any payment and expenditure schedules or plans provided in the original award; explain any major deviations from these schedules; and discuss actions that will be taken to address the deviations.

D. EQUIPMENT AND REAL PROPERTY MANAGEMENT

Is a review of a firm's property management system usually required?

No, the IPA needs to review the property management system only if:

- There is Federally owned property associated with the award; or
- The firm charged the full purchase price of any equipment or real property as project costs (i.e., to Federal funds or the firm's funds that are counted toward required cost sharing); and
- The award under which the property was purchased provides for a continuing Federal interest in the property.

Note that the IPA generally will not need to review the property management system because most DOE awards will

not have Federally owned property associated with them and will allow the firm to charge to the project only depreciation or use charges for real property or equipment.

What are the objectives of the review?

The objectives are to determine whether the firm:

- Obtained the necessary prior approval for the equipment or real property purchase from the contracting officer.
- Keeps proper records for equipment and adequately safeguards and maintains equipment.
- Handles disposition or encumbrance of equipment or real property acquired under DOE awards in accordance with the applicable requirements.

What are the compliance requirements for Federally owned property and for equipment or real property purchased under DOE awards?

To protect the Federal interest in property, the DOE Assistance Regulations include standards for the firm's property management, use, and disposition, as shown in this table:

If the property is ...	Then the property management standards for the for-profit firm are in ...
Real property or equipment purchased under a TIA,	Section 603.685 of 10 CFR part 603.
Federally owned property,	Section 603.690 of 10 CFR part 603.

Note that a for-profit firm may include the full acquisition cost of real property or equipment as a charge to the project only with the prior approval of the contracting officer. The title to the real property or equipment vests conditionally in the for-profit firm upon acquisition, and there is a continuing Federal interest in the property unless a contracting office has statutory authority to do otherwise and elects to use that authority for a particular award. The Federal Government recovers its interest in the property through the disposition process at the project's end.

E. PROGRAM INCOME

Is an audit of program income usually required?

No, most awards will not involve any program income.

What is program income?

Program income is gross income earned by the recipient that is generated by a supported activity or earned as a result of the award. For example, if the purpose of an award is to support the firm's delivery of services and the firm collects fees for doing so, those fees are program income. As another example, if samples of materials or biological specimens are generated as a result of a supported RD&D effort, and the firm sells samples to other RD&D organizations, the proceeds of those sales would be program income. If authorized by the terms and conditions of the award costs incident to the generation of program income may be deducted from gross income to determine program income, provided these costs have not been charged to the award.

What is the objective of this portion of the audit?

The objective is to determine whether program income is correctly recorded and used in accordance with the award terms and applicable standards.

What are the applicable standards for program income?

The standards for program income are in section 603.835 of 10 CFR part 603.