

DEPARTMENT OF VETERANS AFFAIRS

Nonprofit Research and Education Corporations



2013 Annual Report

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I. BACKGROUND

In 1988, Congress passed Public Law (P.L.) 100-322 [now codified at sections 7361-66 of title 38, United States Code (U.S.C.)], which permitted the Secretary of Veterans Affairs (VA) to authorize the establishment of Nonprofit Research Corporations (NPC) at VA medical centers (VAMC). This laid the foundation for the creation of unique partnerships to conduct VA-approved research. P.L. 100-322 allowed the establishment of private, state-chartered, nonprofit entities to provide flexible funding mechanisms for the administration of funds, other than those appropriated to VA, for the conduct of VA-approved research.

II. NPCs' ROLE IN SUPPORT OF VA RESEARCH AND EDUCATION

In 1999, Congress expanded the NPCs' authority to include support for VA's education and training missions. The fundamental purpose of NPCs is to serve Veterans by supporting VA research and education in order to improve the quality of care that Veterans receive.

Beyond administering research projects and education activities, the NPCs support a variety of VA research infrastructure and administrative expenses. They have provided seed and bridge funding for investigators, staffed animal care facilities, funded recruitment of clinician researchers, paid for research administrative and compliance personnel, supported staff and training for institutional review boards, and much more.

III. NPC LOCATIONS

VAMCs throughout the country have long recognized the benefit of establishing NPCs to help support the conduct of VA-approved research and education activities. During 2013, there were 83 NPCs located in 44 states, Puerto Rico, and the District of Columbia. All of the NPCs filed annual reports. NPCs in Huntington, West Virginia; Martinez, California; and New Orleans, Louisiana, reported little or no financial activity this fiscal year. However, they all have assets and are reactivating. During 2013, there were 70 research and education NPCs and 13 research-only NPCs. As shown in the table below, the NPCs vary greatly in size:

Revenues Range	# of NPCs (2013)	# of NPCs (2012)	# of NPCs (2011)	# of NPCs (2010)	# of NPCs (2009)	# of NPCs (2008)
Below \$500K	27 (33%)	32 (41%)	25 (32%)	29 (35%)	29 (35%)	25 (31%)
\$500K- \$1M	15 (18%)	10 (11%)	13 (16%)	14 (17%)	13 (16%)	16 (20%)
\$1M- \$ 10M	34 (41%)	33 (41%)	34 (43%)	34 (40%)	32 (39%)	34 (42%)
\$10M & Above	7 (8%)	6 (7%)	7 (8%)	7 (8%)	8 (10%)	6 (7%)
Total NPCs	83	81	79	84	82	81

Note: 2012 and 2011 data does not include NPCs that were inactive.

IV. ANNUAL REPORTING

Under title 38, U.S.C., section 7366(b), NPCs must submit to the Secretary of VA a detailed statement of their operations, activities, and accomplishments during the previous year.

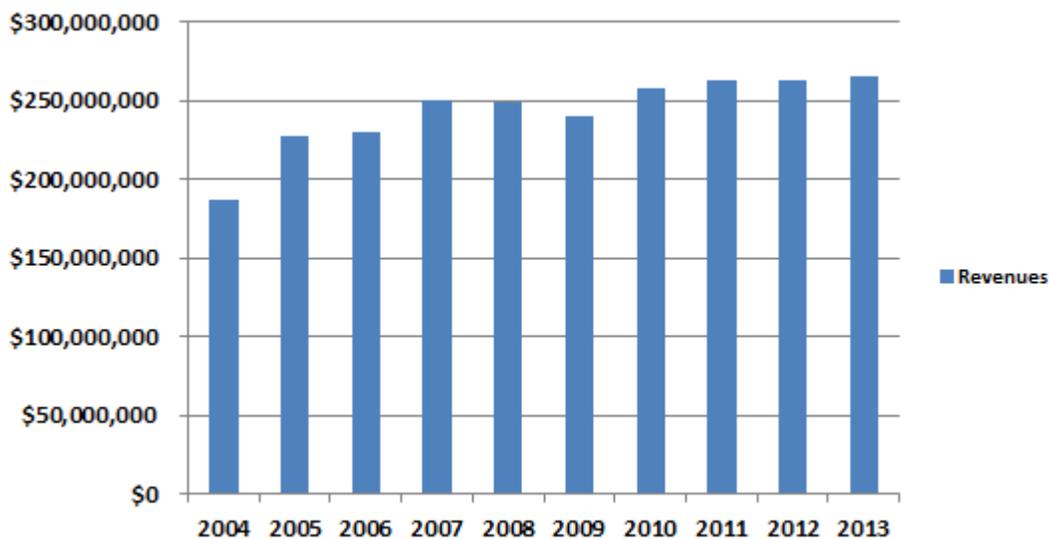
Veterans Health Administration (VHA) *Handbook 1200.17, VA Nonprofit Research and Education Corporations Authorized by Title 38 U.S.C., Sections 7361 through 7366*, dated December 8, 2010, requires each NPC to submit an annual report to VA's Chief Research and Development Officer on or before June 1 of each year. VA's Nonprofit Program Office (NPPO), located in VHA's Office of Research and Development (ORD), reviews the NPC annual reports and is responsible for summarizing the information for the NPC annual report to Congress. The information submitted by NPCs consists of, but is not limited to, Internal Revenue Form 990 – *Return of Organizations Exempt from Income Tax*, audited financial statements, auditor's management letter (if applicable), and related revenue and expense information.

V. FINANCIAL REPORTING

Revenues

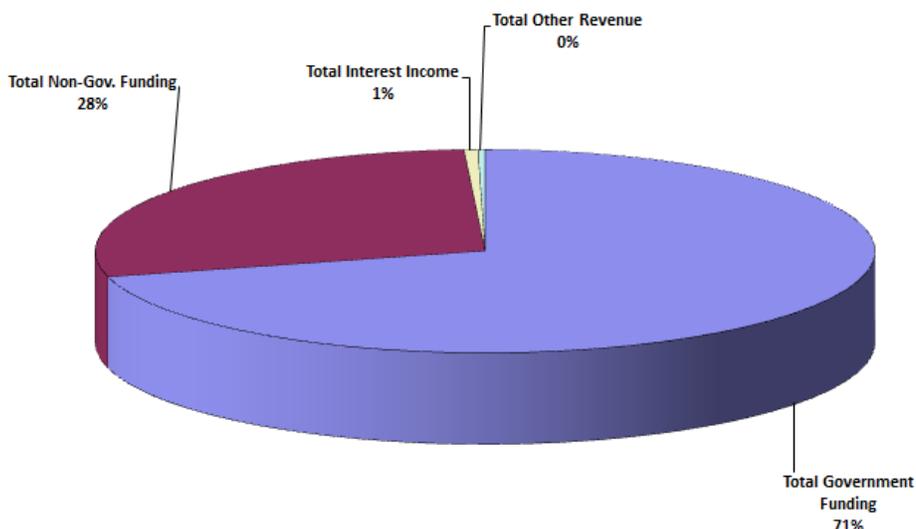
In June 2014, NPCs reported \$264,931,382 total revenues during the 2013 reporting period including interest income and other miscellaneous receipts. This represents a 0.68-percent increase in NPC revenues over the previous year. From 2000 to 2007, total NPC revenue trended up, but revenues decreased in 2008 and 2009. Revenues increased substantially in 2010 and 2011, but were flat for 2012. Forty-seven NPCs reported an increase in overall revenues in 2013 compared to 42 in 2012. For 2013, 35 NPCs experienced declines in revenues.

NPC Annual Revenues – 2004 to 2013



Under the title 38 statutory reporting requirements, NPCs are required to report research and education revenues and expenditures separately. In addition, they must report revenues based on governmental or non-governmental (private) funding sources. Ninety-eight percent of total revenue was received in support of research, while one percent was received in support of education. The remaining one percent was received from other sources such as interest income.

2013 NPC Revenues by Funding Source



As in the previous year, revenue from governmental research and education sources comprised the largest component of funding received by NPCs (approximately 71 percent). In 2013, governmental funding increased to \$187.8 million, or by \$3.1 million (1.6 percent), from \$184.7 million in 2012.

Revenue from non-governmental sources decreased by 1.5 percent from the 2012 amount of \$76.0 million to \$74.9 million for 2013. Other revenue sources (such as interest income) decreased from \$2.5 million in 2012 to \$2.3 million in 2013.

In 2013, the number of NPCs reporting revenue from governmental sources (including VA) was 61, an increase from 54 NPCs reporting governmental revenue in 2012.

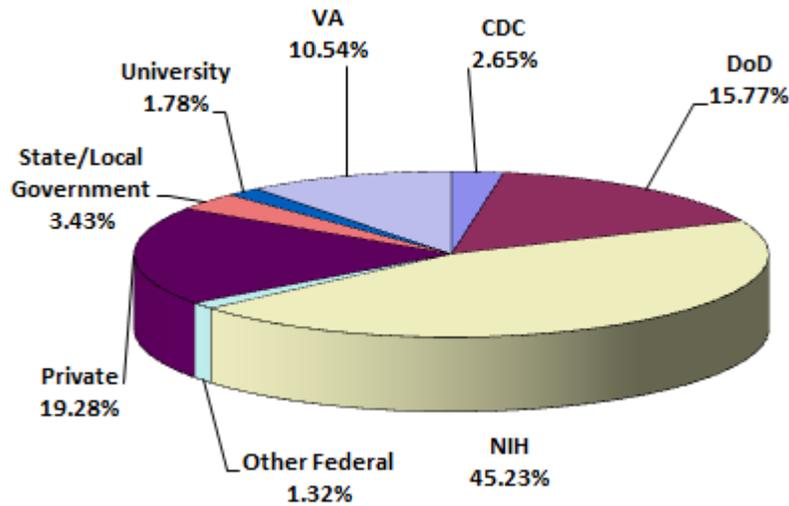
Funding Sources

NPCs continue to obtain funding from diverse sources, including private sector companies, charitable foundations, private individuals, state and local governments, universities, and Federal entities such as the National Institutes of Health (NIH), Department of Defense, and Centers for Disease Control and Prevention.

Funds coming to NPCs from VA are for Intergovernmental Personnel Act (IPA) assignment agreement reimbursements, or are funds from another agency or private entity that have been passed through VA to NPCs.

NPCs are required to identify the funding sources for both governmental and non-governmental amounts greater than \$25,000 (see chart below for the breakdown). For 2013, the total revenue received from these sources was \$237.4 million.

2013 Revenues >\$25,000 by Funding Source

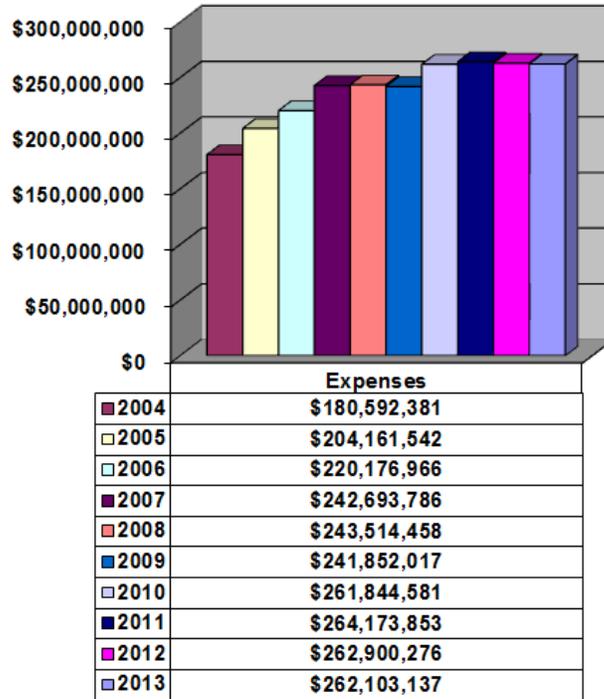


Expenses

In June 2014, NPCs reported expenses totaling \$262,103,137 during 2013, a decrease from 2012 expenses which were \$262.9 million. These expenses financed research projects and their supporting infrastructure as well as salaries, equipment, and other research and education-related costs. The NPCs employed approximately 2,700 people, supported 2,300 principal investigators, and administered 3,500 research projects.

Because the statutory purpose of NPCs is to facilitate VA research and education, all funds spent must support those activities with the exception of amounts that cover NPC administration.

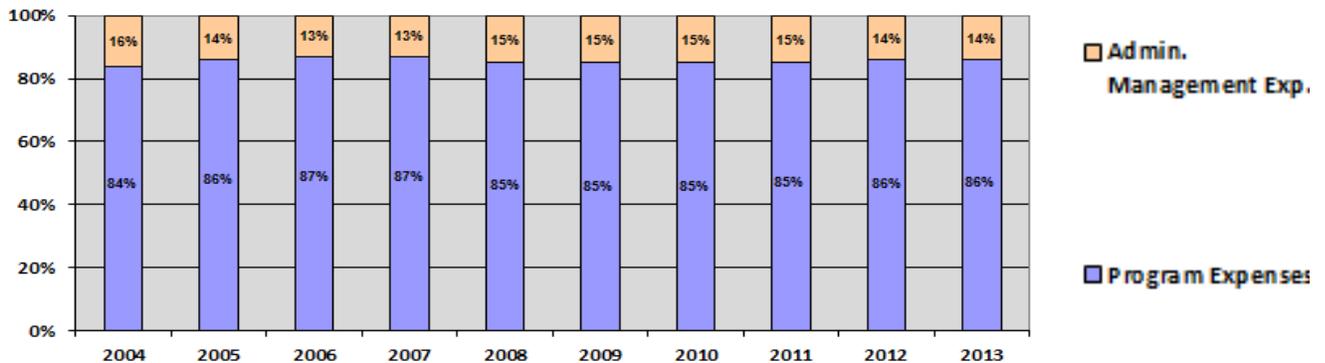
NPC Annual Expense 2004-2013



During 2013, approximately 55 percent of total expenses covered salaries and benefits, approximately 2 percent of total expenses covered travel, and the remaining 43 percent represented other expenses in direct support of VA research and education activities or NPC business operations.

NPCs continue to spend a relatively small amount on administrative expenses, averaging 14 percent (\$36.6 million) of total expenditures for 2013.

NPC Total Combined Administrative Management Expenses vs. Direct Program Expenses 2004-2013

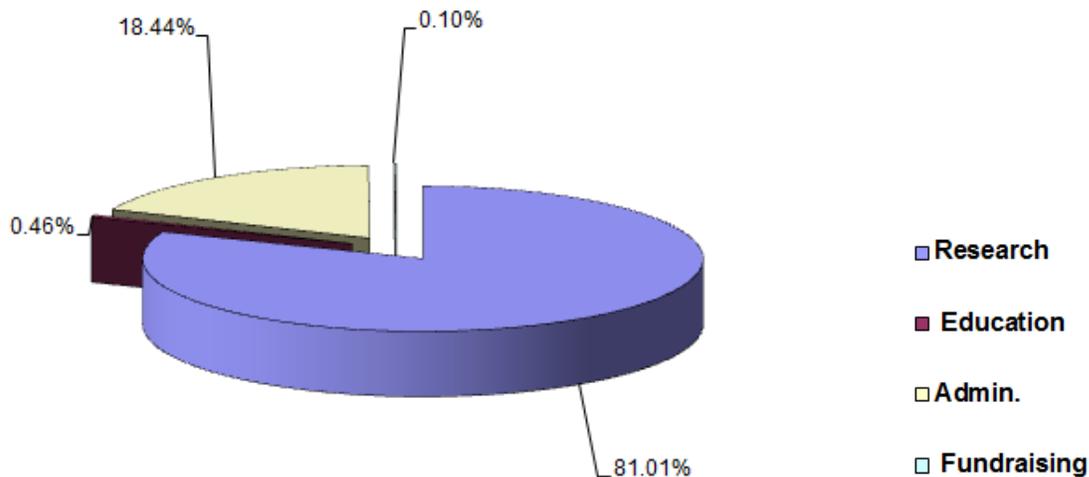


Compensation Expense

During 2013, 78 NPCs reported compensation expenses including benefits totaling \$144.1 million, a 0.6-percent decrease over 2012. NPC salary expenditures supported a variety of personnel (including research technicians, pharmacists, scientists, nurses, physicians, and administrative staff).

Of the \$144.1 million spent for compensation, 81 percent (\$116.8 million) was used to support personnel directly engaged in VA research. Approximately 18.4 percent (\$26.6 million) was expended for NPC administrative salaries. Less than one percent (\$666,596) was expended in support of staff involved in educational activities.

2013 Compensation Expense by Category

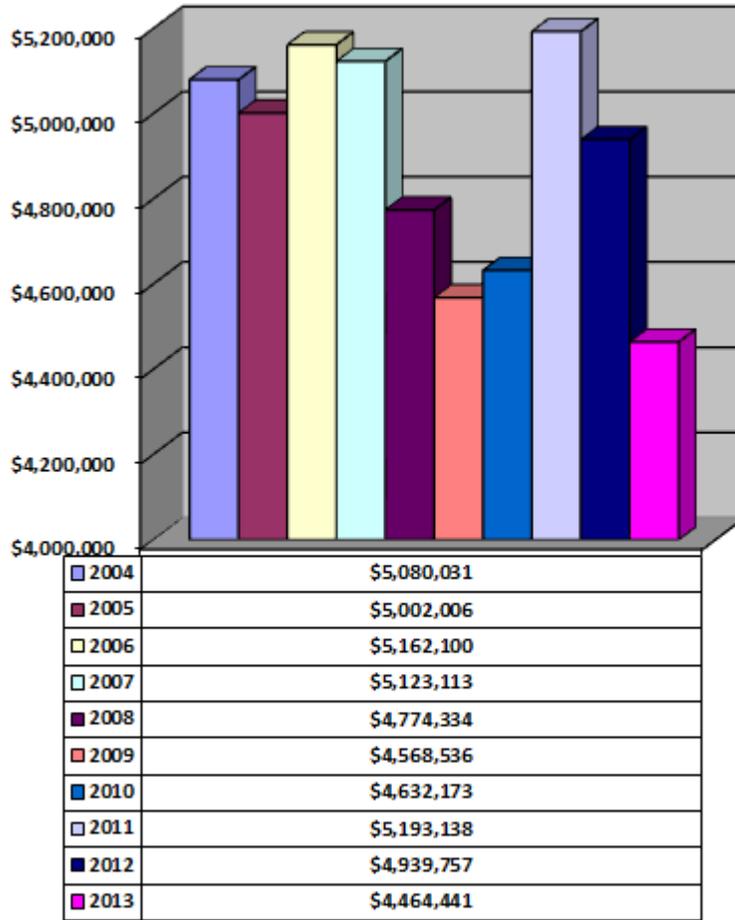


Travel Expense

NPCs support travel for VA and NPC personnel to attend scientific and educational meetings, seminars, and conferences. VA benefits from such travel because it enhances the ability of VA staff to pursue research and education endeavors important to VA's health care, training, and research missions. Seventy NPCs reported travel expenditures totaling \$4.5 million, an 8-percent decrease from \$4.9 million in 2012.

Of the \$4.5 million in travel expenditures, approximately 80 percent, or \$3.6 million, supported travel for personnel directly engaged in research or education activities.

NPC 2013 Total Travel Expense



Other Expenditures

While furthering VA’s research and education missions, NPCs incur a number of costs in addition to payroll, benefits, and travel. During the 2013 reporting period, other expenses totaled \$113.5 million, up by 0.4 percent from \$113.0 million in 2012. They included, but were not limited to, legal fees, insurance, accounting, auditing, consulting services (statisticians, information technology experts, etc.), supplies, postage, shipping, equipment purchases, rentals and maintenance, printing, publications, utilities, and conference registrations.

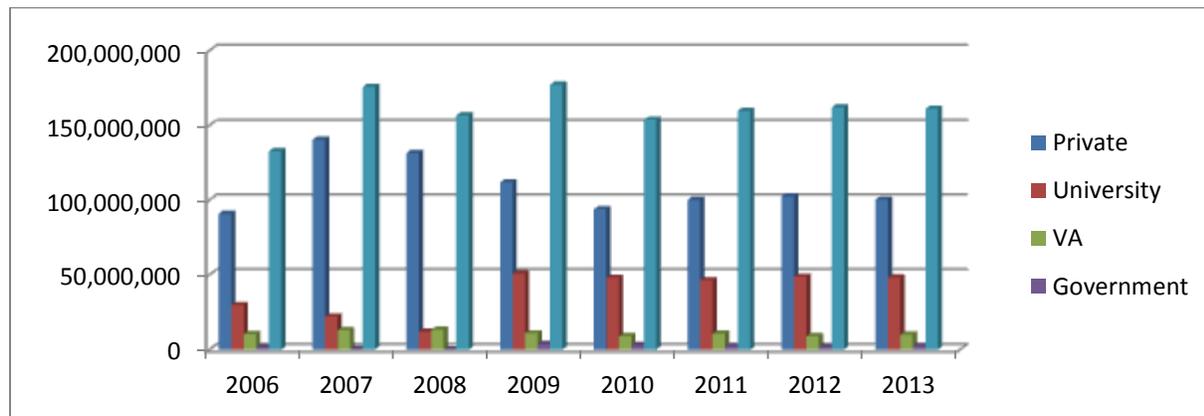
Payees

Each NPC hires employees and contracts with various vendors (“payees”) to support the conduct of VA-approved research and education activities.

The vendors provide products and services that sustain research, education, and business operations. Any payee receiving in excess of \$50,000 per year is identified in the NPC report. The table lists the four major types of payees and provides the total amount paid to each type. Private payees include employees,

consultants, etc. State and private university payees may include reimbursements from grants or sub-awards. VA reimbursements are costs reimbursed in support of VA research and education activities. Other governmental payees include sub-awards or pass-through funds to non-VA government entities.

**Chart of NPC Payees Greater than \$50K (\$35K before 2010)
by Type 2006-2013**



<u>Payee Types</u>	<u>2006</u>	<u>2007</u>	<u>2008</u>	<u>2009</u>	<u>2010</u>	<u>2011</u>	<u>2012</u>	<u>2013</u>
Private	90,844,058	140,387,974	131,335,642	111,959,281	93,884,222	100,027,918	102,474,233	100,327,510
University	29,697,260	22,109,633	11,942,527	50,842,649	48,014,076	46,354,923	48,662,749	48,186,773
VA	10,380,024	12,899,309	13,213,619	10,834,080	8,901,718	10,653,349	8,939,402	10,044,013
Government	1,696,321	284,595	186,338	3,590,256	2,993,649	2,518,859	1,844,892	2,538,045
Totals	\$132,617,663	\$175,681,511	\$156,678,126	\$177,226,266	\$153,793,665	\$159,555,049	\$161,921,276	\$161,096,341

Financial Position

NPCs reported net worth totaling \$204,409,854 at the end of 2013, a 1.7-percent increase from the 2012 net worth, which was \$200.9 million. Gross assets under management were \$268.2 million and liabilities were \$63.8 million. The ratio of net worth to revenues was 77 percent for all of the NPCs. For the top 20 NPCs that comprised 78 percent of total revenues, the net worth ratio was 55 percent. Some individual large NPCs had substantially lower ratios than the average and have been advised to conserve their net worth as best they can and to augment when possible.

VI. PROJECTS, ACTIVITIES, AND ACCOMPLISHMENTS

NPCs facilitated a variety of projects during the 2013 reporting period. Many of these research projects were clinical studies that focused on the treatment of medical conditions prevalent in the Veteran population. Veterans benefit from getting access to cutting edge pharmaceuticals and medical care devices. Many Veterans who participate in VA studies benefit not only from the actual “hands on” care provided, but also indirectly from the interaction between NPC staff and patients.

The quality of care given to Veterans enrolled in clinical studies is exceptional and is a direct result of the close one-on-one relationships between the caregivers

conducting the research and the Veterans. VAMCs may benefit from drugs and devices donated by sponsoring institutions and pharmaceutical companies. VAMCs also benefit from NPC salary support for nurses and physicians caring for Veteran patients enrolled in clinical studies.

NPCs also support VA in many different ways beyond administering funds. Examples are listed below:

- Renovate and upgrade VA research infrastructure;
- Provide funds, staffing, and training support to VA and affiliate universities to help cover Institutional Review Board requirements;
- Pay for expenses related to recruitment of research investigators to the VA system;
- Fund seed grants to new investigators to aid them in establishing their VA research careers;
- Employ support staff for VA research projects;
- Cover the cost of training VA research personnel in topics such as research compliance, good clinical practice, and board governance;
- Underwrite bridge funding for VA investigators who are between research grant awards;
- Support travel and registration fees for VA investigators to attend scientific conferences;
- Procure personnel, equipment, and supplies for VA animal research facilities;
- Provide funds for research pharmacy staff and equipment; and
- Host national educational conferences for VA personnel with incidental attendance by health professionals from surrounding communities.

VII. CONFLICTS OF INTEREST

NPC directors, officers, and employees are subject to the conflict of interest policy adopted by that NPC. VA employees who serve as NPC directors as part of official VA duty are also subject to the Federal conflict of interest laws and regulations. The Federal conflict of interest laws and regulations govern if there is a conflict with NPC policy for VA employees who serve as NPC directors.

VIII. VA NONPROFIT PROGRAM OVERSIGHT BOARD

In 2004, VA senior leadership created the VA Nonprofit Program Oversight Board to serve as VA's senior management oversight body over NPC activities and programs. The Board meets on a quarterly basis to review the activities of the NPCs for consistency with VA policy and interests. The Board may also make recommendations to the Secretary and Deputy Secretary concerning changes to, and implementation of, VA policy regarding NPCs. Board membership is limited to VA employees and includes:

- Under Secretary for Health;
- General Counsel;
- Assistant Deputy Under Secretary for Health for Operations and Management;

- Chief Research and Development Officer;
- VA Nonprofit Program Officer;
- Chief Academic Affiliations Officer;
- Chief Financial Officer for VHA, or a designee;
- Member, Office of Research and Development Field Research Advisory Committee; and
- Chief Officer, VA Office of Research Oversight.

IX. INDEPENDENT AUDIT REPORTS

NPPO reviews the independent audit reports and the related audited financial statements for the NPCs. The NPPO also reviews other documents such as the independent audit management letters, lists of program activities and accomplishments, and supplemental revenue and expenditure information. This oversight is performed in order to obtain substantive evidence of accountability and to have a balanced picture of NPC program activity.

Any material weaknesses or significant deficiencies in internal controls and related recommendations made by the NPCs' independent auditors are noted. NPPO tracks these from year to year to determine whether the NPCs have taken the appropriate corrective actions as recommended by their independent audits.

Under title 38 U.S.C. section 7366(b), each NPC with annual revenues in excess of \$500,000 is required to obtain an independent audit of its financial statements for the year. NPCs with annual revenues between \$100,000 and \$500,000 must obtain an audit every 3 years. External audits were not required for 18 NPCs in 2013. Of the 83 NPCs, 65 (78.3 percent) submitted audited financial statements. For 2013, 99.2 percent of total NPC revenues and 99.1 percent of total expenses were subject to independent audits.

There are three ascending levels of independent audits:

- (1) Generally Accepted Auditing Standards (GAAS) in the United States of America Audit: This audit requires the auditor to plan and perform the audit in order to obtain reasonable assurance that the financial statements are free of material misstatements. The auditor assesses internal controls, management, and governance. An NPC receiving more than \$100,000 but less than \$500,000 in funding is required to obtain, at a minimum, an audit in accordance with GAAS once every 3 years.
- (2) Generally Accepted Government Accounting Standards (GAGAS) Audit: This audit also obtains reasonable assurance that the financial statements are free of material misstatements. The GAGAS audit is used when required by provisions of laws, regulations, contracts, and grants.
- (3) Circular A-133 Audit: This audit is performed in accordance with Office of Management and Budget (OMB) Circular A-133, when annual expenditures are from Federal funds exceeding \$500,000. The A-133 audit is designed to

provide assurance that the financial statements are reasonable and there is compliance with the legal and regulatory requirements of the Federal contract(s) and grant(s), and with sound internal controls.

The table below is a summary schedule of independent audits performed in 2013.

Type of NPC Audits Performed in 2013					
	A-133	GAGAS	GAAS	No Audit Report	Total
Number of Audits	31	2	32	18	83
Total Revenue	\$225.4M (85.1%)	\$ 3.0M (1.1%)	\$34.6M (13%)	\$2.0M (0.7%)	\$265.0M
Total Expenses	\$222.2M (84.8%)	\$2.9M (1.1%)	\$34.7M (13.3%)	\$2.3M (0.9%)	\$262.1M

Six NPCs were cited by their auditors for material weaknesses. All of these material weaknesses are different than those reported in 2012. The NPCs with material weaknesses are working closely with NPPO and their external auditors to ensure correction of the weaknesses prior to the next audit. NPPO requires an in-depth action plan from each NPC with material weaknesses and follows up on these during on-site reviews.

Five of the NPCs reporting material weaknesses were audited under GAAS and one was audited under an A-133 audit. The NPPO will follow up to ensure these material weaknesses and other deficiencies are corrected. The Executive Director of each NPC is responsible for providing a copy of the auditor's report to the NPC's Board of Directors and involving the Board directly in the resolution of any deficiencies. The NPPO has written to each of these NPCs requesting a remediation action plan.

X. NPPO OVERSIGHT PLAN AND RESULTS

NPPO is charged with conducting oversight for the 83 VA affiliated nonprofit research and education corporations nationwide. NPPO reviews and discusses the Operations Oversight Questionnaire and the Internal Control Questionnaire with the Executive Director during our on-site visit. NPPO routinely tests samples of various transactions and accounting records, such as policies and procedures, cash disbursements, credit card purchases, bank statements and reconciliations, payrolls, and IPA assignment agreements.

The limited on-site reviews by NPPO are for the purpose of providing audit, investigative, and oversight-related services that do not involve a GAGAS full financial, attestation, or performance audit examination. NPPO's limited reviews are not designed to detect fraud, waste, abuse, or other irregularities. NPPO's reviews are substantially narrower in scope than an audit examination. The objective of an audit examination is the expression of an opinion on the subject matter, and accordingly, no such opinions are expressed. *Ref. Government Auditing Standards 2011 Revision, Chapters 2.12 and 5.56, Pages 19 and 116.* Nonetheless, NPPO

reserves the right to extend its limited reviews; initiate other reviews or investigations; and arrange for the conduct of complete GAGAS financial, attestation, or performance audits if needed for effective VHA oversight. NPPO observes auditing standards set by the Comptroller General of the United States.

1. All NPCs will be reviewed triennially regardless of financial condition. To accomplish this, one-third of the NPCs are audited each year.
2. NPCs with identified operating problems or serious internal control weaknesses will be reviewed on site annually and monitored. Once the issues are resolved and NPC receives a satisfactory review, its review schedule will be moved to the triennial schedule.
3. New Executive Directors (ED) are greeted and welcomed and are notified of the new ED workshop, the NPPO Web site, and staff contact information within the first 45 days of employment.
4. NPCs that are starting up, reactivating, merging, or deactivating will be visited as needed.
5. NPCs with reported irregularities (e.g., by whistleblowers) will be reviewed on site immediately and have appropriate follow-up action taken.
6. NPCs requesting on-site visits to resolve internal control, financial systems, or financial management problems will be visited as soon as possible.

All 83 NPCs have been reviewed by NPPO. Formal review reports were prepared for each of these reviews.

In addition to the routine triennial reviews, NPPO has performed many non-routine whistleblower complaint, timekeeping, and fraud investigations.

Other routine oversight conducted at NPPO offices includes reviews of:

1. Annual reports due June 1 on forms prescribed by NPPO.
2. Annual audited financial statements due to NPPO by June 1.
3. Annual Form 990 income tax returns due to NPPO by June 1.
4. Remediation plans for all NPCs with material weaknesses reported by their independent auditors.
5. Remediation plans for all NPCs with significant deficiencies and auditor recommendations.
6. Monthly financial statements compared to budget and last year for NPCs with identified operating problems and/or inadequate reserves.

7. Immediate attention to all NPC requests for assistance or advice.

XI. NPPO TRAINING

Over the past 4 years, NPPO has:

1. Developed and facilitated a 2-day workshop for Executive Directors.
2. Developed training courses designed for VA's Talent Management System for mandatory courses:
 - a. Internal Controls.
 - b. Conflict of Interest.
3. Provided extensive training sessions for the boards of directors as part of the on-site oversight reviews.
4. Maintained an easy-to-navigate, user friendly and informative Web site.
5. Developed a PowerPoint training for the proper completion of Intergovernmental Personnel Act assignment agreements.

XII. CONCLUSION

VA-affiliated NPCs continue to make a substantial contribution to VA research and education missions. The 2013 NPC Annual Report to Congress demonstrates that NPCs are fulfilling their Congressional mandate in a responsible and conscientious manner.

Expertise in NPC governance and management is improving as evidenced in the on-site reviews and the NPCs' annual reporting to VA. VA-affiliated NPCs contribute significantly to the success of VA's research and education programs.

This report and the NPPO's on-site reviews illustrate that the NPCs are a highly efficient means to maximize the benefits to VA of externally funded research conducted in VA facilities. NPCs greatly facilitate research and education that benefit Veterans. Additionally, NPCs foster vibrant research environments at VAMCs, enhancing VA's ability to recruit and retain clinician-investigators and other talented personnel who apply their knowledge to state-of-the-art care for Veterans.