

Cost Allocation and Indirect Costs

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Costing Options:

1. Direct Charge
2. Cost Allocation Plan (CAP)
3. Indirect Costs / Facilities and Administrative (F&A) Costs



Direct Cost Allocation Principles

- ◆ Cost that is easily assigned to an award / cost objective
 - ◆ E.g., Employee works 100% on program activity
- ◆ Costs that benefits more than one program / cost objective in a way that “can be determined without undue effort or cost”
 - ◆ E.g., Employee works on Grant A 50% of the time; and Nonfederal activities 50% of the time
- ◆ 2 CFR 200.405(d)

Direct Cost Allocation Principles

- ♦ But – what if it’s not easy to allocate costs because of the interrelationship of the work involved??
 - ♦ “[T]he costs may be allocated or transferred to benefitted projects on any reasonable documented basis.”

- ♦ 2 CFR 200.405(d)

For example ...

- ♦ Purchase a multipurpose business center (printer, copy, scanner, shredder, etc.) for \$3,500
- ♦ Used in office shared by Grant A, Grant B, and Grant C



For example ...

Cost Allocation:

- ♦ Grant A: \$1,166
- ♦ Grant B: \$1,166
- ♦ Grant C: \$1,166



For example ...

But, what if Grant A has 5 FTEs, Grant B has 10 FTEs, and Grant C has 3 FTEs?

Cost Allocation based on FTEs:

- ♦ Grant A: \$972
- ♦ Grant B: \$1,944
- ♦ Grant C: \$583

For example ...

But what if the grantee puts a use-code on the machine and tracks use by Grant for 3 months, determining that Grant A uses the machine 15%, Grant B uses the machine 45%, and Grant C uses it 30%?

Cost Allocation based on usage:

- ♦ Grant A: \$525
- ♦ Grant B: \$1,575
- ♦ Grant C: \$1,050

“[T]he costs may be allocated or transferred to benefitted projects on any reasonable documented basis.”

- ♦ 2 CFR 200.405(d)

What about a cost that provides the same / equal benefit to two programs – how do you allocate?



Direct Cost Allocation

- ♦ “A State or subgrantee may use funds under more than one program to support different parts of the same project if the State or subgrantee meets the following conditions:
 - ♦ The State or subgrantee complies with the requirements of each program with respect to the part of the project assisted with funds under the program
 - ♦ The State or subgrantee has an accounting system that permits identification of the costs paid for under each program.”
- ♦ 34 CFR 76.760

For example ...

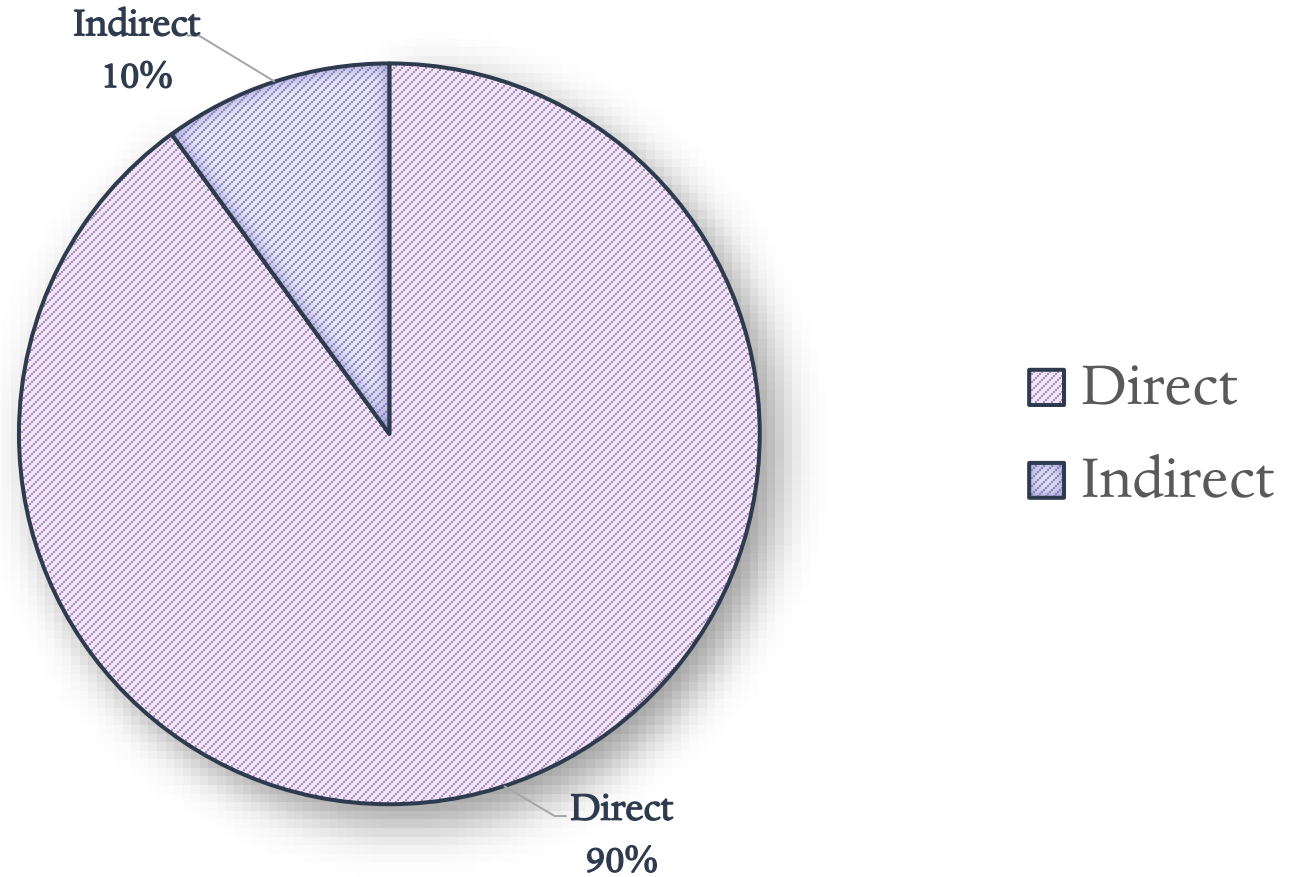
- ◆ District plans a leadership workshop for school principals to help address post-pandemic challenges and learning loss.
- ◆ Allowable under Title II and ESSER
- ◆ The District has discretion on how to fund the workshop; it could be: (1) fully charged to Title II, (2) fully charged to ESSER, or (3) charged to both programs in whatever proportions the District chooses.

English Please!

- ◆ If a cost is *fully* allowable under two programs, the grantee can make a business decision on how to fund it. It need only track the money from each program that is spent on the cost.

Indirect Costs

Total Cost of Federal Awards



What Is The Purpose Of The Indirect Cost Rate?

- ♦ Allows agency to recover some costs incurred to run federal programs that are otherwise too integrated to identify
- ♦ Take portion of grant as “recovery”; treat as non-federal funding.
- ♦ Creates tension in agency because reallocates funds from the program



How To Get An Indirect Cost Rate?

- ♦ Non-federal entities apply to “cognizant agency”
- ♦ Unless specified by OMB, generally the “cognizant agency” is the federal agency with the preponderance of direct funding
- ♦ “Cognizant agency” authority may be delegated to *nonfederal* agencies
 - ♦ For example, SEAs have methodology approved through “delegation authority” from ED. LEAs must apply to SEA.
 - ♦ Post-secondary and nonprofit subgrantees receive “restricted” rates from the SEA.

FAQ 1: Can I charge _____ as an indirect cost?

Classifying costs as direct vs. indirect.

- ◆ “There is no universal rule for classifying certain costs as either direct or indirect.”
 - ◆ 2 CFR 200.412
- ◆ But...there are guidelines

What are Direct Costs?

- ♦ Costs that can be identified specifically with a particular final cost objective
- ♦ “Cost objective” means a function, organizational subdivision, contract, grant, or other activity for which cost data are needed and for which costs are incurred
 - ♦ Ex.: Compensation of employees for effort on the performance of the award; materials and equipment; travel expenses.

What are Indirect Costs?

- ◆ Costs incurred for common or joint purposes
- ◆ Cost cannot be readily and specifically identified with a particular cost objective without effort disproportionate to the results achieved
 - ◆ Ex.: Accounting; Human Resources; Payroll; Legal Division; Utilities
 - ◆ 2 CFR 200.1



What are Indirect Costs?

- ♦ “Administration” is defined as general administration and general expenses such as the director’s office, accounting, personnel, and all other types of expenditures not listed specifically in “Facilities”
 - ♦ Nonprofits – includes library expenses
 - ♦ IHEs – library expenses included in “Facilities”
- ♦ “Facilities” is defined as depreciation on buildings, equipment and capital improvement, interest on debt associated with certain buildings, equipment and capital improvements, and operations and maintenance expenses
 - ♦ Appendix III, B. 1.

Selected Items of Cost – Classification as Indirect Costs

- Depreciation is the required method for allocating the cost of fixed assets to periods
 - Use Allowance method no longer allowed
- Unused leave payments must be charged indirectly, 200.431(b)(3)(i)*
- Actual claims for workers comp, unemployment compensation, severance pay, and similar employee benefits are allowable provided that they are allocated as indirect costs, 200.431(e)(3)*
 - *If nonfederal entity uses cash basis of accounting or if nonfederal entity uses specific identification for fringe benefits, then not required to charge these costs indirectly
 - **But, state/local governments that use cash basis of accounting still must charge termination leave “as a general administrative expense to all activities of the governmental unit or component” (i.e., indirectly)

Wait...there's more

- ♦ For programs with supplement not supplant provision, must use a **Restricted Rate**
- ♦ Under restricted rates, indirect costs are defined as:
 - ♦ **General Management Costs:** activities for the direction and control of the grantee's affairs that are organization-wide
 - ♦ Excluding:
 - ♦ Divisional administration limited to one component of grantee
 - ♦ Governing body of the grantee
 - ♦ Compensation of the chief executive officer of the grantee
 - ♦ Compensation of the chief executive officer of any component of the grantee, and
 - ♦ Operation of the immediate offices of these officers
 - ♦ EDGAR 76.565

General Management Costs

- ♦ Two prong definition:
 - ♦ (1) Organization-wide
 - ♦ (2) Direction and control of the organization
- ♦ For example...
 - ♦ Grant writers, even if considered “proposal costs” (must proportionately support both federal and non-federal activities within the agency)
 - ♦ Curriculum development, pupil data, library services, evaluation services, and school services (although cross-cutting, not for the “direction and control of the organization” – rather provide services to schools or students)

General Management Costs

- ♦ What are “component” costs?
 - ♦ Generally, organizational units “one management level below the executive office”
 - ♦ Component heads and their direct reports are adjusted
 - ♦ Org chart is key!



English Please!

- ◆ Sometimes costs incurred for common or joint purposes and that cannot be identified with a specific cost objective (meeting the UGG definition of “indirect”), could not be classified as indirect costs under a restricted rate (fail to meet “general management” definition).



Case Study:

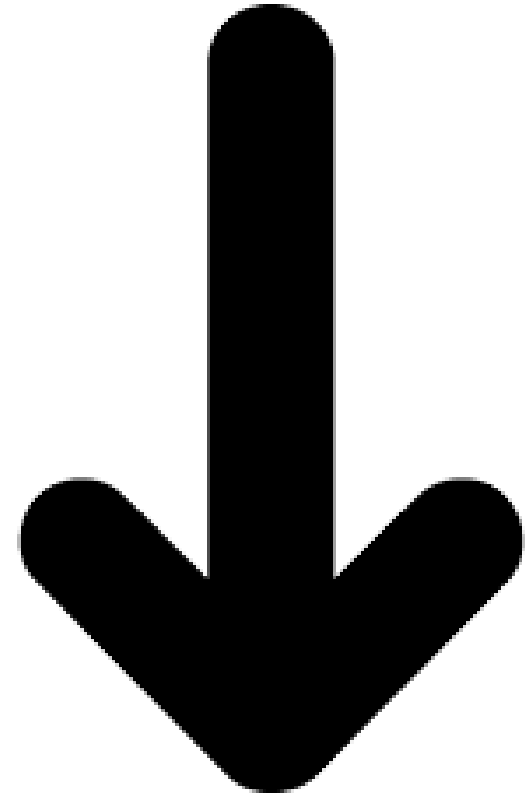
Alabama Dept of Rehab Services

- ♦ Computer Services (IT) Unit works across major programs and sub-programs, that include approximately 54 different grants or other revenue sources
- ♦ ED Indirect Cost Division: Must be allocated as a direct cost per 200.405(d) based on job descriptions that show percentage of time spent on IT-related duties.
- ♦ ADRS: But 200.405(d) says we can use any reasonable, documented basis. Therefore, propose all Computing Services be allocated as indirect costs. 200.1 defines indirect costs as those that would be otherwise too burdensome to directly allocate. IT is exactly like that; the costs, burden, and effort associated with direct charging IT is disproportionate to the benefit.

Case Study:

Alabama Dept of Rehab Services

- ♦ ED Indirect Cost Division: Decided 19 of the 36 employees in the unit should be direct charged, so moved to base. This reduced the approved rates from 12.3 to 10.3% (unrestricted) and from 10.3 to 8.4% (restricted).
- ♦ Deputy Assistant Secretary for Acquisition and Grants Administration: received the appeal request and upheld the ICD determination.



FAQ 2: When (and why) do I have to exclude contract costs over \$25k?

Applying the indirect cost rate.

Charging Indirect Costs to Federal Awards

- ◆ Calculation: It's a fraction!!
- ◆ Top: "Indirect Cost Pool"
- ◆ Bottom: "The Base"
 - ◆ Can be "Total modified direct cost base" or "Salaries and Wages", etc.



Top: Indirect Cost Pool

- ♦ Ex.: Accounting; Personnel; Legal; Utilities
- ♦ All employees must be paid with non-federal funds (even though giving *some* benefit to federal programs)
 - ♦ Would not keep time distribution records (as long as not split between indirect and direct)
- ♦ Must show benefit to federal program

Bottom: “Modified Total Direct Cost Base”

- ♦ All direct costs (All federal and non-federal expenses)
- ♦ Minus “distorting items”



Applying the Rate

- ◆ Apply rate (percentage) *to the base* (apply to your current year direct costs minus capital expenditures, etc., NOT entire grant!)
- ◆ That “reimbursement” has no federal accountability ... or does it ???

Hunter College Settlement

- ♦ False Claims case brought against a professor, Parsons, and Hunter College related to use of NIH Grant funds.
- ♦ Hunter used recovered indirect cost funds to pay Parsons over \$90,000 of retention bonuses.
- ♦ Hunter did not disclose the use of the indirect recovery for such bonuses to NIH.



Hunter College Settlement (cont.)

- ♦ “Although Hunter had wider discretion in how it could utilize the Indirect Cost Funds as compared to NIH grant funds, Hunter could not use the Indirect Cost Funds in any manner that contradicted its certifications in the Indirect Cost Agreements.”
- ♦ In its certifications, Hunter agreed “that the Indirect Cost Funds were ‘subject to any statutory or administrative limitations,’ including the statutes, regulations, and rules that prohibited NIH funds from being used for unallowable expenses.”
- ♦ Settlement for \$200,000 (includes findings related to time and effort, as well).

Wrong Way / Right Way: Modified Total Direct Cost Base (MTDC)

<u>Incorrect Calculation</u>	
Total Award	\$4,000,000
	<u><u>\$4,000,000</u></u>
Rate Applied	20%
Indirect costs	\$800,000

<u>Correct Calculation</u>	
Total Direct Costs	\$3,350,000
Less: Equipment	(\$100,000)
Less: Subcontract	(\$2,550,000)
Plus: first \$25,000	<u>\$50,000</u>
MTDC Base	<u><u>\$750,000</u></u>
Rate Applied	20%
Indirect costs	\$150,000

Applying the Rate - Frequency

- ♦ Can claim indirect costs periodically (monthly, quarterly, annually)
- ♦ Must be based on actual expense already incurred (i.e., couldn't take all at beginning of year)

Exclusions from MTDC Base (200.1)

- ◆ Equipment
- ◆ Capital Expenditures
- ◆ Charges for patient care
- ◆ Rental costs
- ◆ Tuition remission
- ◆ Scholarships and fellowships
- ◆ Participant Support Costs
- ◆ Subawards in excess of \$25,000
- ◆ Other items with approval of cognizant agency for IC

Definition of “subaward” (200.1)

- ♦ An award provided by a pass-through entity to a subrecipient. “It does not include payments to a contractor...”



What ED says...

- ♦ “When we talk about subawards, we are talking about subgrants and subcontracts. ... We have to look at it on a case-by-case basis.”
- ♦ Whether the portion over \$25k will be excluded “depends upon the amount of administrative handling involved in that subaward or subgrant.”
- ♦ ED links to DOL’s guide:
 - ♦ As a general rule ... only the first \$25,000 of each subcontract, subgrant and professional service agreement should be included in the distribution base. This recognizes that grantees/contractors expend a minimal amount of indirect costs on subcontracts.

Cost Allocation Guide

- ♦ Subawards
 - ♦ Grantee hires individual to perform speech pathology services to students in school, is this a “subaward”?
 - ♦ No, although professional service, this auxiliary expertise is normally provided in-house
 - ♦ Grantee hires school nurse that provides medication (not an instructor) to students in class, is this a “subaward”?
 - ♦ No, although professional service, this auxiliary expertise is normally provided in-house
 - ♦ Grantee contracts with software vendor to provide technical support and enhancement of existing business software, is this a “subaward”?
 - ♦ No, organization-wide support, this is an indirect cost

English Please!

- ♦ Federal agencies, including ED, have interpreted “subawards” broadly to include certain professional service agreements as distorting items that must be excluded. Therefore, whether the amounts above \$25,000 under certain contracts must be excluded from the calculation and recovery of indirect costs will depend on your approved rate, as negotiated with the awarding agency.
- ♦ What about multi-year subawards/contracts?
 - ♦ May apply the \$25,000 once within the period of performance

FAQ 3: If admin is capped at 5%, must my ICR also be capped at 5%?

The relationship between indirect and admin.

Administration vs. Indirect

- ♦ Administrative costs may be direct *or* indirect
- ♦ **If a grant has an administrative cost cap, the limit applies against total grant amount**
- ♦ Grantee should list administrative costs in budget breakout

Administration vs. Indirect

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Administration vs Indirect

All indirect are administrative costs

Cost Allocation Guide, 2019

OCTAE Monitoring reports, 2018

Whether indirect is “administrative” depends on the underlying direct cost

Past practice

Prior Indirect Cost Director

EANS Guidance, 2021

EANS Guidance:

Are indirect costs subject to the administrative cap?

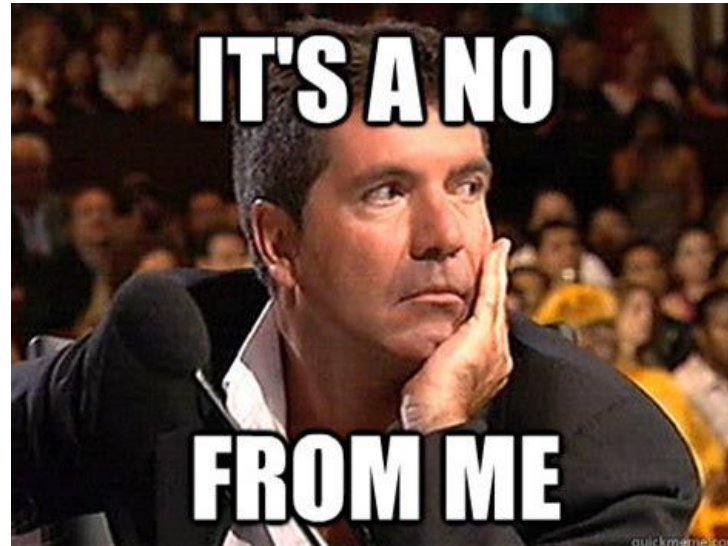
- ♦ “Whether an indirect cost is an administrative cost subject to an SEA’s cap on administrative costs depends on the nature of the direct costs to which the indirect cost applies. If, for example, an SEA incurs indirect costs that are associated with administration of the EANS program, those indirect costs would be subsumed within the SEA’s administrative cost cap. On the other hand, if an SEA incurs indirect costs associated with providing actual services or assistance to non-public schools, the indirect costs would not be administrative costs and would not be charged against the SEA’s administrative cap.”

EANS Guidance (cont.)

- ♦ Email to Indirect Cost Director (2021):
- ♦ “For example, if a state agency applies its indirect cost rate to direct cost activities under the Perkins State Leadership set-aside, are the associated indirect costs included in that set-aside, or must the associated indirect be subject to the Perkins administrative cost limitation? (There were a series of audits by OCTAE a few years ago that indicated indirect applied to state leadership would be subject to the state admin cap.) Similarly, if an LEA has a cap on admin of 5%, must the LEA include all of its recovered indirect against that cap, or could it – consistent with the EANS guidance above – treat the indirect costs associated with providing direct services as programmatic costs not subject to the admin cap.”

EANS Guidance (cont.)

- ♦ Response from Indirect Cost Director (2021):
- ♦ “EANS is a unique program because the basis is to provide assistance associated with COVID-19 hardships and the FAQs that are program specific shouldn’t be extrapolated to other programs.”



What were we talking about again?

FAQ 3: If admin is capped at 5%, must my ICR also be capped at 5%?

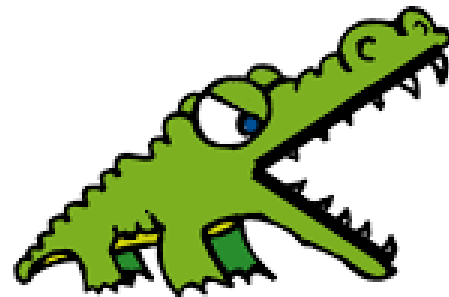
The relationship between indirect and admin.

For example:

- ◆ Perkins subgrant has 5% cap on admin
 - ◆ Post-secondary subgrantee has 8% restricted rate
- ◆ Perkins subgrant = \$100,000
 - ◆ Grantee spent entire award
 - ◆ \$50,000 went toward equipment, distorting items
- ◆ Applying the rate: $\$50,000 * 8\% = \$4,000$
 - ◆ Even if all indirect costs are “administrative”, grantee still does not exceed 5% cap in applying 8% rate.

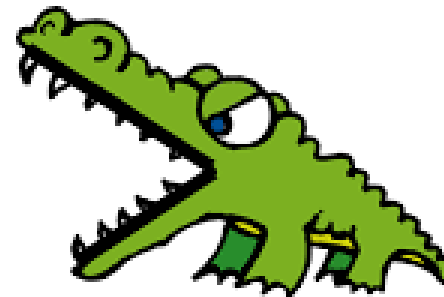
So the answer is...?

- ♦ Not necessarily. If admin is capped at 5%, the grantee may still apply a higher indirect cost rate. However, recovery of indirect administrative costs and direct administrative costs must be within the 5% cap.



Less Than Gator

VS



Greater Than Gator

One more thing before we move on...

Direct v. Indirect Costs Administrative Costs

- Salaries of administrative and clerical staff should be treated as “indirect” unless all of following are met:
 1. Such services are integral to the activity
 2. Individuals can be specifically identified with the activity
 3. Such costs are explicitly included in the budget
 4. Costs not also recovered as indirect
- 2 CFR 200.413(c)

Other questions?

- ◆ Does a pass-through entity have to negotiate an indirect cost rate with a subrecipient?
- ◆ Can a pass-through entity cap indirect cost rates?
- ◆ Who can use the de minimis rate?
- ◆ Are contractors entitled to their indirect cost rate?
- ◆ Do I have to claim indirect costs? Can I claim indirect on only certain grants?

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