

## SECTION II

### Guidelines for Preparing Indirect Cost Rate Proposals

Note: Grantees/Contractors must have an established accounting system prior to being awarded a grant or contract from DOL or any other agency in the Federal government. The accounting system must provide adequate internal controls to safeguard assets, insure fund accountability by cost category, assure accounting data accuracy and reliability, promote operating efficiency, and comply with Government requirements and accounting procedures.

For reference purposes, see the Standards for Financial Management Systems in [OMB Circular A-110](#). Also, see evaluation of accounting systems referenced in [FAR Part 9.106](#) and the [Standard Form 1408](#).

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This section includes the following information:

- A. Preliminary Steps
- B. Indirect Cost Allocation Bases
- C. Indirect Cost Rate Proposal "Checklist", and Notes to "Checklist"
- D. Indirect Cost Proposal – Review Procedures
- E. Administration Limits and Indirect Cost Claims

#### A. Preliminary Steps

Prior to the preparation of an indirect cost rate proposal and supporting documentation, the cost principles established by OMB Circular A-122 (2 CFR Part 230) for grantees or the Federal Acquisition Regulation (Part 31.2) should be thoroughly reviewed. If indirect costs are allowed in the award, the entity will then be ready to prepare an indirect cost rate proposal based on the following steps:

##### 1. Organization Review

- If one does not already exist, prepare a formal organizational chart(s), or a rough draft version, and provide any information or material explaining the various services and/or functions for each unit.
- Determine which units are indirect (administrative) functions of the organization.
- Determine the services that are allowable and allocable to Federal grants and contracts, using guidance provided in OMB Circular A-122 (2 CFR Part 230), or if applicable, FAR Part 31.

##### 2. Review Federal and Non-Federal Funding

- Review the "Federal and Non-Federal Outlays" to determine programs being funded; verify with the appropriate staff.
- Prepare a list of all funded programs in detail as to the amount or percent of reimbursement of direct and indirect cost and any restrictions or references to statutes or regulations.
- Determine at what organizational level the various funded programs apply. Illustrate the list of funded programs on a copy of the organization chart.
- Contact the Federal agency which provides the most funds regarding the procedures for the submission, review and approval of indirect cost rates.

### **3. Review the Accounting Structure**

- Obtain a chart of accounts, or some other list of accounts for your organization, in which the actual dollars expended can be related to various programs and/or organization structure.
- Reconcile the accounting structure to the organization chart.
- If necessary, determine changes to implement an indirect cost rate system of billing.

### **4. Prepare a Cost Policy Statement**

- Develop a written policy that outlines the costs considered as direct, the costs considered to be indirect, and the rationale to support those costs. A sample cost policy statement is available in Section III.

### **5. Prepare an Indirect Cost Rate Proposal**

- Determine which method is best for the organization, i.e., direct cost allocation or simplified, and whether special indirect cost rates are required, i.e. on-site, off-site, fringe benefit rate for full-time vs. part-time. In selecting the appropriate method, the organization should consider the following:
  - a. Organizational structure
  - b. Level of Federal funding
  - c. Reports generated from their accounting system
  - d. Availability of data on square footage, number of transactions, employees, purchase orders, etc.
  - e. Additional effort and cost required to achieve a greater degree of accuracy.
- Prepare the indirect cost rate proposal following the examples shown in Section III.
- Prepare a Certificate of Indirect Costs and have signed by the Executive Director, or other designated official with organization's signature authority (see Section III for a sample).
- Compile all remaining documentation required by the cognizant Federal agency – for DCD organizations see DCD's checklist on page II-4.
- Reconcile the indirect cost rate proposal to the audited (if applicable) financial statements.

### **6. Obtain Cognizant Agency Approval**

- Submit proposal to cognizant agency;
- Cognizant agency may follow up after review with questions, and/or concerns – and may request additional documentation, and/or narrative responses, in support of the proposal.
- Document meeting and/or telephone conversations, e-mails and faxes.
- Make any agreed upon changes, and submit any revised, and/or supporting documentation requested by cognizant agency.
- Receive Negotiated Indirect Cost Rate Agreement.

### **7. Implementation**

- Prepare claims using the lower of either the approved rate, or the ceiling rate for your grant or contract.
- Use final rate(s) included in indirect cost rate agreement for close-out purposes.
- Maintain documentation for audit purposes – see page I-4 for Retention of Records.

## B. Indirect Cost Rate Allocation Bases

The following allocation bases are acceptable examples for use when indirect costs are allocated to benefiting cost objectives by means of an indirect cost rate. (Also see Exhibit E Suggested Allocation Bases – pages III-12 & III-13)

1. Direct salaries and wages including (or excluding) all fringe benefits.
2. Direct salaries and wages including vacation, holiday, sick pay, and other paid absences but excluding all other fringe benefits.
3. Total direct cost excluding (if applicable) capital expenditures (buildings, individual items of equipment; alterations and renovations), subawards or that portion of each subaward in excess of \$25,000 and flow-through funds.
4. Total direct costs excluding (if applicable) capital expenditures (buildings, individual items of equipment; alterations and renovations); subawards or that portion of each subaward in excess of \$25,000; rental/maintenance of off-site activities; student (enrollee) tuition payments and student support costs (e.g. student aid, stipends, dependency allowances, scholarships, fellowships).
5. Modified total direct costs consisting of salaries and wages, fringe benefits, materials and supplies, services, travel, and subawards up to \$25,000 each or all subawards.

**NOTE: The cost of equipment purchases, major renovation or subcontract costs may vary considerably from program to program which causes the indirect cost to be allocated in a disproportionate amount to the benefit derived. Therefore, such costs will be excluded from the base when a total direct cost is being used.**

6. For commercial entities, total costs less G&A expenses.

The selection of an appropriate allocation method should be based upon the commonality of costs to all cost objectives. In general, a correlation exists between the incurrence of administrative effort with the expenditures for direct labor. In most cases, a direct labor base will produce an equitable distribution of indirect costs. However, where the ratio of direct labor to total direct costs varies significantly from program to program, an "adjusted" total direct cost base should be used in allocating costs to benefiting programs.

The proposed allocation base(s) is subject to negotiation and approval by DCD. Any modifications to the "approved" base require prior written approval. Failure to obtain such written approval may result in cost disallowance.

### C. Indirect Cost Rate Proposal Checklist – non-profit and commercial organizations<sup>1</sup>

<p>1. Submit <u>once</u> unless changes are observed:</p> <p>___ 1a. Organizational chart,</p> <p>___ 1b. Employee time sheet sample, providing for distribution of hours to direct/indirect functions.</p> <p>___ 1c. Signed Cost Policy Statement.</p> <p>2. An Indirect cost rate proposal(s) providing the following:</p> <p>___ 2a. <u>Personnel Costs Worksheet</u>, including fringe benefits breakdown.</p> <p>___ 2b. <u>Allocation of Personnel Worksheet</u>, providing indirect/direct time charges.</p> <p>___ 2c. <u>Fringe Benefits Worksheet</u>,</p> <p>___ 2d. <u>Statement of Total Costs</u>, supporting the indirect and direct costs incurred by expense category, identified by Federal agency, specific government grant, contract, and other <u>non-government</u> activities.</p> <p>___ 2e. <u>Statement of Indirect Costs</u>, including indirect cost pool(s), allocation base(s), and indirect cost rate(s) proposed.</p> <p>3. ___ Audited financial statements, if available. If audited financial statements are not available, IRS Form <u>990</u> (non-profits) or compilation/review financial statements (for-profits) for the final rate proposal. Approved budget for provisional proposal, if needed. OMB A-133 supplemental information, if available. <u>Note</u>: The Statement of Total Costs (2d. above) must reconcile to Financial Statements. If not, please provide documentation showing reconciliation.</p> <p>4. ___ Certification that the indirect cost rate proposal was:</p> <p>___ 4a. prepared in a manner consistent with the applicable cost principles set forth in OMB A-122 for non-profits, or the Federal Acquisition Regulations (Part 31) for commercial organizations.</p> <p>___ 4b. that the non-profit grantee complied with the lobbying requirements of OMB Circular A-122 (2 CFR Part 230), Attachment B, paragraph 25 (If applicable).</p> <p>The certifications must be signed by the President/Executive Director, or Comptroller/ CFO.</p> <p>5. ___ A listing of grants and contracts by Federal agency, total dollar amount, period of performance, and the indirect cost (overhead) limitations (if any) applicable to each, such as, ceiling rates or amounts restricted by administrative or statutory regulations, applicable to the period(s) of the proposal(s). This listing should <u>also</u> be supported by the approved federal grant or contract notification award(s).</p>
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<sup>1</sup> Refer to Section III of this guide or to the following website to obtain samples of indirect cost proposal exhibits, employee timesheet, certification and cost policy statement:  
<http://www.dol.gov/oasam/programs/boc/costdeterminationguide/main.htm>

## Notes to “Checklist”, as applicable

1a. Not applicable.

### **1b. Timesheet or Personnel Activity Report (PAR)**

An acceptable timesheet or PAR sample is available in Section III of this Guide.

### **1c. Cost Policy Statement (CPS)**

An example of a CPS is shown in Section III of this Guide.

The CPS is a disclosure of the organization’s accounting practices, policies, and procedures for allocating direct and indirect costs. It is required documentation upon an organization’s first indirect cost rate proposal submission and requires a signature.

DCD requires its’ Cost Negotiators to review an up-to-date CPS as part of the review process upon submission of an indirect cost rate proposal. If applicable, for subsequent proposals, organizations need only identify changes made from the original CPS.

If the contractor/grantee is not proposing any changes, the following suggested language should be included in the transmittal letter when a proposal is submitted:

**[ABC Non-Profit/Commercial Organization] hereby confirms that no changes to its accounting policies and practices as set forth in its Cost Policy Statement dated [September 13, 200X] have been made.**

### **2a. Personnel Costs Worksheet**

An example of a personnel costs worksheet is presented as Exhibit A in Section III of this Guide.

When preparing a Provisional Indirect Cost Rate Proposal, current approved budget figures should be used in the preparation of the personnel costs worksheet. When a Final Indirect Cost Rate Proposal is prepared, actual personnel costs should be used in preparation of this Exhibit.

Actual personnel costs should be documented in accordance with OMB Circular A-122 (2 CFR Part 230), Attachment B, paragraph 7.m. (1) through (4), and the FAR.

### **2b. Allocation of Personnel Worksheet**

An example of an Allocation of Personnel Worksheet is shown in Section III, Exhibit B of this Guide.

This document reflects the estimated or actual salary costs for each Federal and Non-Federal cost objective. The percentage of time per position should be entered under the appropriate cost objective, making sure that 100 percent is allocated for each position.

The grantee/contractor must maintain a time distribution system for use by employees whose time is charged to more than one cost objective. Payroll documentation should be maintained to support the charging of salaries and wages as direct or indirect.

**2c. Statement of Employee Benefits**

An example of a Statement of Employee Benefits is shown in Section III of this Guide.

This document should contain the estimated or actual costs of the items in the employee fringe benefit pool. Employee (fringe) benefits should follow the salary of the individual and are a consideration in the determination of the reasonableness of the compensation. Fringe benefits should be accrued in the period incurred, including accrued leave if employees have an irrevocable right to be compensated during employment or upon termination of employment.

Generally, the cost of annual leave is recognized when it is earned by the employee, and holiday and other types of leave are considered a cost to the extent of actual compensation to employees.

**2d. Statement of Total Costs**

Examples of the Statement of Total Costs (STC) are shown in Section III of this Guide; Exhibits D or E, for the simplified method or direct allocation method, respectively (see top portion in yellow).

This document should contain all line items of costs included in the entities' chart of accounts (and CPS) with applicable columns for direct costs (by cost center), indirect costs, (overhead, G&A, etc.) and unallowable costs (if applicable).

The total costs should reconcile to the entities' financial statements. If it does not reconcile, the entity should provide a separate schedule supporting all differences.

**2e. Statement of Indirect Costs**

Examples of the Statement of Indirect Costs (as part of the STC) are shown in Exhibits D or E, for the simplified method or direct allocation method, respectively (see bottom portion of spreadsheets shown in blue and green).

This document should contain all line items of costs included in the indirect cost "pool(s)", the applicable allocation base(s), and the resulting indirect cost rate(s).

The allocation base should be traceable to the statement of total costs. If it is not clearly traceable, an additional schedule should be provided to supporting the reconciliation.

**4. Certificate of Indirect Costs**

The required certificate is shown in Section III of this Guide.

A "Certificate of Indirect Costs" must be signed on behalf of the organization, by an individual at a level no lower than executive director or chief financial officer of the organization that submits the proposal.

**5. List of Grants and Contracts**

A sample spreadsheet showing a list of grants and contracts is available in Section III of this Guide.

## D. Indirect Cost Proposal – DCD’s Review Procedures

Some issues that may be raised by a DCD negotiator during, or after, the review of an indirect cost rate proposal, usually result from the following procedures. Knowing these procedures while preparing an indirect cost rate proposal, organizations may enable us to avoid such issues from occurring.

- Determine that the applicable cost principles (stated in the Circulars or the FAR) were followed.
- Review the organization chart for a visual picture of the flow of responsibility, identification of areas of common costs, and the location of those areas in which federally-funded activity exists
- Perform a mathematical verification of the proposal.
- Determine that the proposal reconciles with the supporting audit, official budget or financial statements.
- Review the financial report for any indication of activities which may have been omitted from the indirect cost proposal, i.e., the omission of restricted fund costs or the existence of an affiliated organization receiving supportive service from the parent organization.
- Determine that the cost centers in the indirect cost pool pertain to functions that are supportive of all direct activity.
- Determine that costs that are statutorily unallowable, or for reasons of non-allocability, have been eliminated from the indirect cost pool. Determine whether these unallowable or non-allocable items should be added to the distribution base.
- Determine that "pass-through" funds have been excluded from the base.
- Review the analysis of direct costs for the determination of:
  - a. Consistency in charging specific items of cost.
  - b. The selection of an appropriate base for allocating indirect costs.
- Review the contract/grant budget and payments, or contractor/grantee records, for a determination of: (if deemed feasible under the circumstances)
  - a. The direct funding of indirect costs.
  - b. Any limitations placed upon the full recovery of indirect costs, i.e. ceiling rates or amounts.
  - c. Total Federal funds involved.
- Check with the appropriate Federal Program Manager for any problems he/she may be aware of relating to the charging of costs.

## E. Administration Limits and Indirect Cost Claims

Various DOL funding instruments have statutory or regulatory limitations on the costs of "administration". These costs can be both personnel and non-personnel and both direct and indirect. The costs of administration are those portions of reasonable, necessary and allowable costs associated with the overall program management and administration and which are not directly related to the provision of services to participants or otherwise allocable to the program cost objectives/categories

Based on the above information, the statutory or regulatory limitation affects the combined claims for indirect costs and direct administration costs. Generally, direct administration costs differ from indirect charges in that the latter are considered organization-wide costs.

Examples of functions that are classified as direct "administration" are as follows:

- Overall **program** management, program coordination, and office management functions, including the salaries and related costs of the executive director, project director, and project evaluator **when directly allocated**.
- Preparing **program** plans, budgets schedules, and related amendments.
- Monitoring of programs, projects, sub-recipients and related systems and processes.
- Developing systems and procedures, including management information systems, for assuring compliance with program requirements.
- Preparing reports and other documents related to the **program** requirements.
- Evaluating program results against stated objectives; and
- Performing administration services such as **program specific** payroll, accounting, auditing or legal activities.

Examples of non-labor costs for direct administration include:

- Costs for goods and services required for administration of the **program**, including such goods and services as the rental or purchase of equipment, utilities, office supplies, postage, and rental and maintenance of office space.
- Travel costs incurred for official business in carrying out **program** management and administrative activities.