

An Overview Indirect Costs



Denver, Colorado - August 2005
USDOL/VETS

Competitive Grantees Training Conference
Presented by Phil Zahnd
Regional Cost Negotiator
Atlanta Region



What will we cover?

- Definitions/Terms
- Who needs a rate and why
- Recovery of costs
- OMB Circular A-122 – general concepts
- Allowable, Allocable and Reasonable costs
- Direct versus Indirect
- Submission of ICR Proposals
- Rate types
- Example of an ICR agreement



Are you loaded down with Federal regulations?



dcd/pz

Are you overburdened with paperwork?



dcd/pz

Dr. Pri

Cannot solve your cost allocation problems!

OMB

Circulars:

www.whitehouse.gov

DCD's Website:

[http://www.dol.gov/oasam/programs/boc/
costdeterminationguide/main.htm](http://www.dol.gov/oasam/programs/boc/costdeterminationguide/main.htm)



Download
Now

Relationship of Circulars

Type of Institution	Cost Principles	Admin Requirements	Audit
State/Local Gov't	A-87	"Common Rule" A-102	A-133
Colleges & Univers	A-21	A-133	A-133
Hosps. & Care Facs	Various, 45 CFR 74	Various, A-133	Various, A-133
Nonprofit	A-122	A-110	A-133
Commercial	31 CFR 15.2	FAR	FAR

History of A-122

- Issued June 27, 1980
- Updated numerous times
- Revised – June 1, 1998
- Revised – May 10, 2004
 - To bring symmetry between Circulars A-21, A-87, and A-122
 - Revisions synchronize most items of cost in the three circulars

Objectives of the Circular(s)

- Feds bear “fair share” of costs
- Provide guidelines for organizations concerning reimbursement requirements
- Provide uniform standards of allowability
- Provide uniform standards of allocation
- Do not supersede limitations imposed by law
- Simplify intergovernmental relations
- Encourage consistency in treatment of costs

Structure of A-122

- Attachment A: General Principles
- Attachment B: Selected Items of Cost
- Attachment C: Non-Profit organizations not subject to this Circular

For nonprofit organizations, the largest dollar volume of direct Federal funding is normally used to determine the cognizant Federal agency. (This may be negotiated between Federal agencies.)

Which organizations need to have an approved indirect cost rate?

\$ Single Funding Source

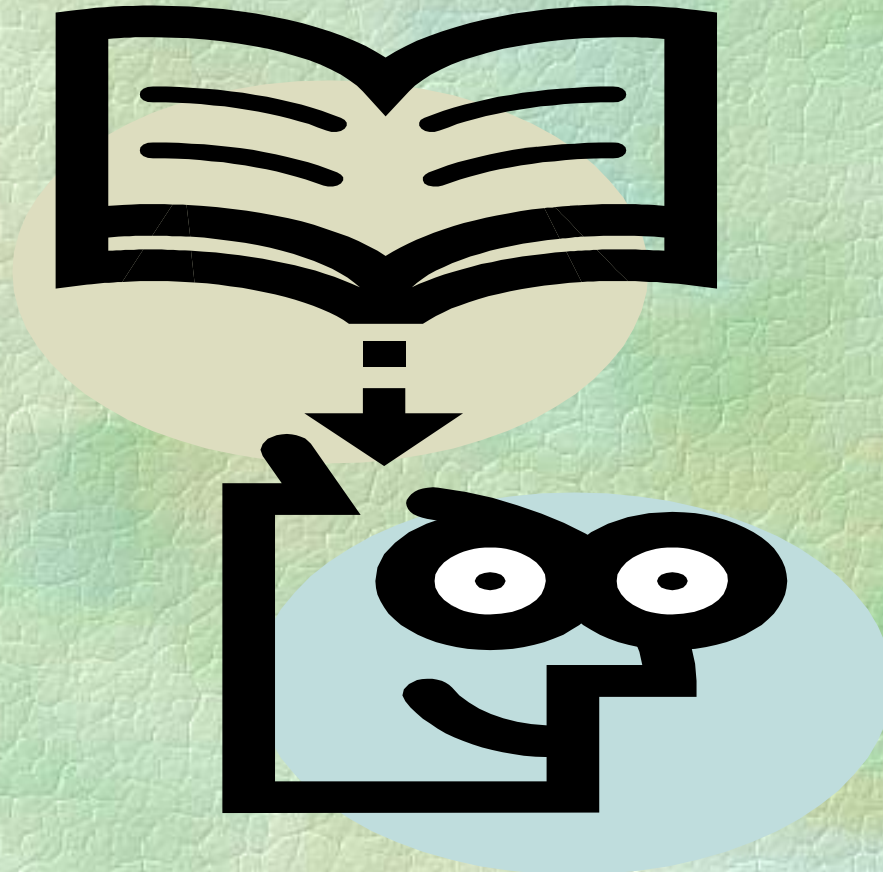
Indirect cost rate not needed

\$\$\$ Multiple Funding Sources

Indirect cost rate needed



Some cost allocation terminology



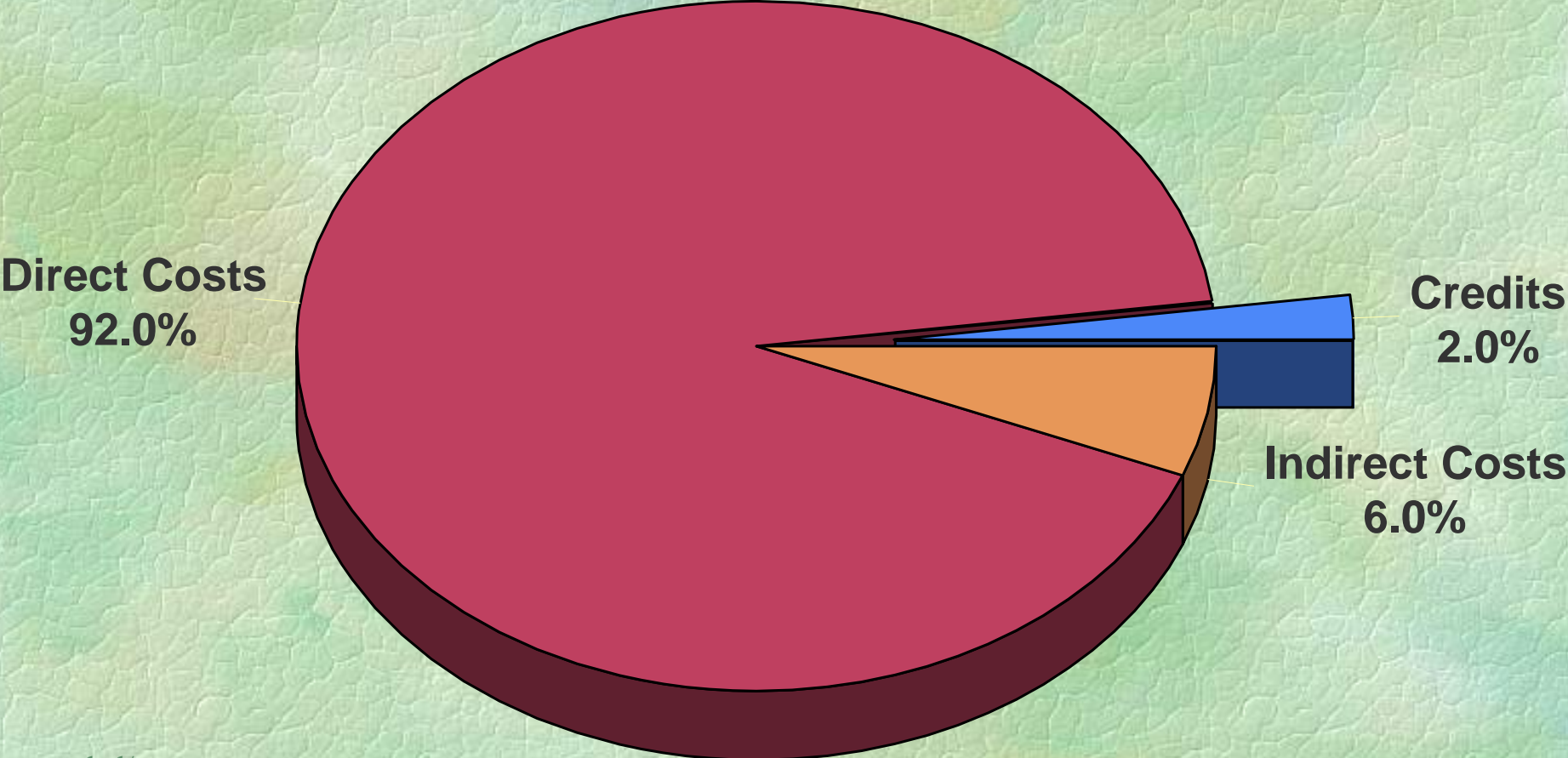
Total Costs =
Direct Costs
Plus
Indirect Costs
Less
Applicable Credits

What are Applicable Credits?

Receipt or negative expenditure types of transactions which operate to offset or reduce expense items that are allocable to grants or contracts as direct or indirect costs. Examples include:

- Purchase discounts, refunds, rebates or allowances
- Sales of scrap or incidental services
- Adjustments of overpayments or erroneous charges

Graphic of Total Costs





What are direct costs?

- Those costs that can be readily identified with a particular cost objective. Examples: (program specific)
 - Salaries – VETS program staff
 - Space – sq. ft. occupied by direct staff
 - Supplies – used by direct staff
 - Communications – used by direct staff



What are indirect costs?

- Those costs which are not readily identifiable with a particular cost objective.

Examples:

- Salaries – Executive Director, Accountant, etc.
- Space – sq. ft. occupied by indirect staff
- Supplies – used by indirect staff
- Communications – used by indirect staff

To be chargeable to a Federal grant/contract, indirect costs must be:

- Allowable
- Reasonable
- Allocable

To be allowable, costs must:

- Be reasonable and allocable
- Conform to any limitations or exclusions set forth in the cost principles or the award
- Be consistent with policies and procedures afforded all activities of the organization
- Be accorded consistent treatment
- Be determined in accordance with GAAP
- Not already be included in a cost sharing or matching requirement
- Be adequately documented

Reasonable Costs

A cost is reasonable if, in its nature or amount, it does not exceed that which would be incurred by a prudent person under the circumstances prevailing at the time the decision was made to incur the costs. Some considerations might be:

- Effect on Federal program dollars
- Prudence under the circumstances
- Deviations from established practices

Allocable Costs

- A cost is allocable to a Federal award if it is treated consistently with other costs incurred for the same purpose in like circumstances and if it:
 - Is incurred specifically for the award
 - Benefits the award and other work and can be distributed based on benefits received, or
 - Is necessary for the overall operation of the organization, although a direct relationship to a particular cost objective cannot be shown
- Shifting of costs between awards to overcome funding deficiencies is not allowed

Allocable Costs (cont'd)

- A cost is allocable to a particular cost objective in accordance with the relative **benefits received**.
- An allocable cost benefits a cost objective -- either directly, or indirectly.
 - Examples: VETS staff salaries, occupancy costs, Fiscal Officer's supplies.

Unallowable Costs

- Specifically identified in the grant/contract as being unallowable
- Specifically identified in Circular A-122 as being unallowable
- Does not meet the criteria listed in Circular A-122 to be allowable

Why talk about this?

Documentation for Compensation

- Because it's usually the largest item of administrative direct/indirect cost under any given DOL grant/contract
- Because it is so often the subject of audit questioned costs



Compensation for Personnel Services

- Must be reasonable and in accord with established practice
- Must be supported in accordance with applicable Circular subsections (support of salaries and wages)

Compensation for Personnel Services(cont'd)

- Charges to Federal awards must be
 - Based on documented payrolls approved by the responsible official of the organization
 - Supported by Personnel Activity Reports (PAR, aka, time distribution report)

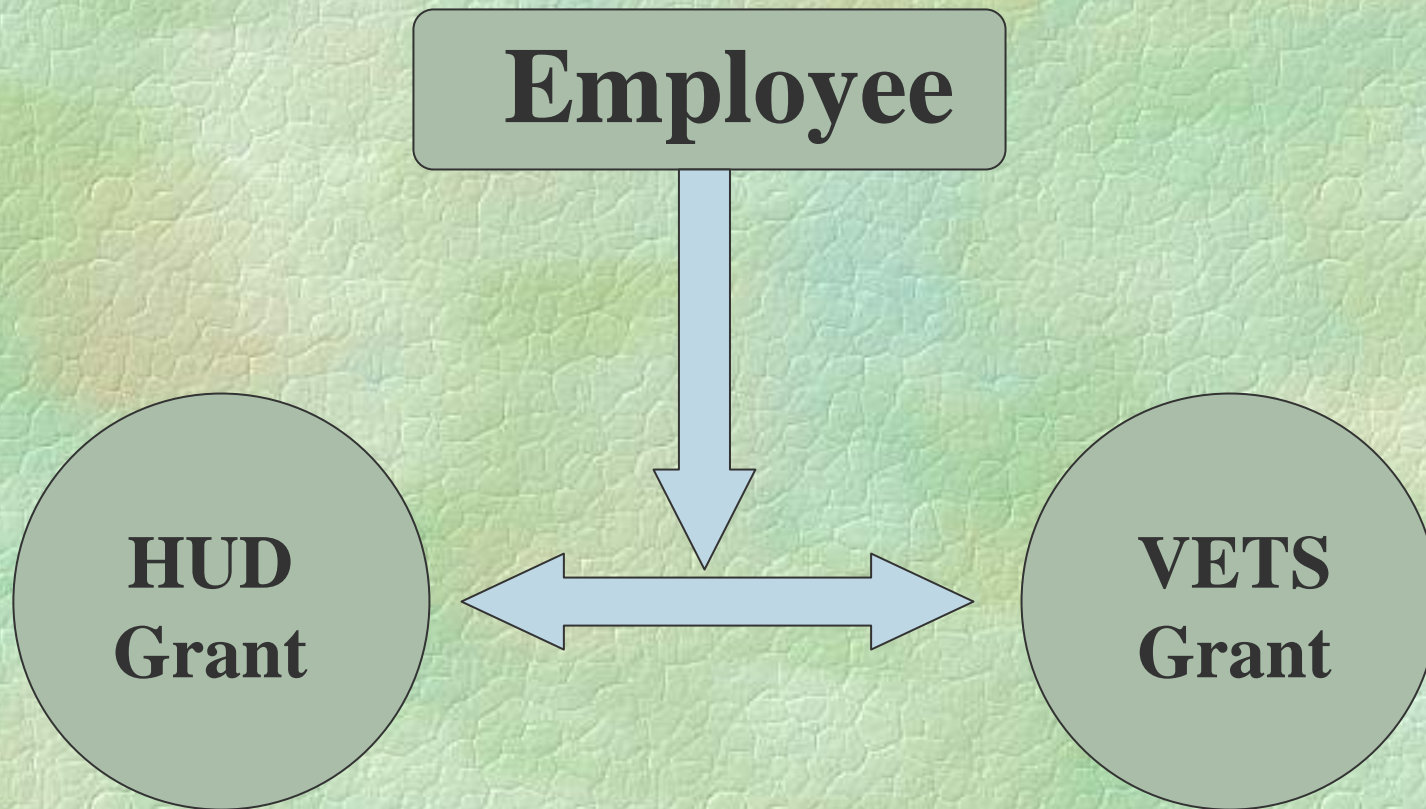
Compensation for Personnel Services(cont'd)

- PARs must meet the following standards
 - Reflect after-the-fact distribution of effort
 - Must account for total activity for which the employee is compensated
 - Must be signed by the employee
 - Be prepared at least monthly and coincide with one or more pay periods

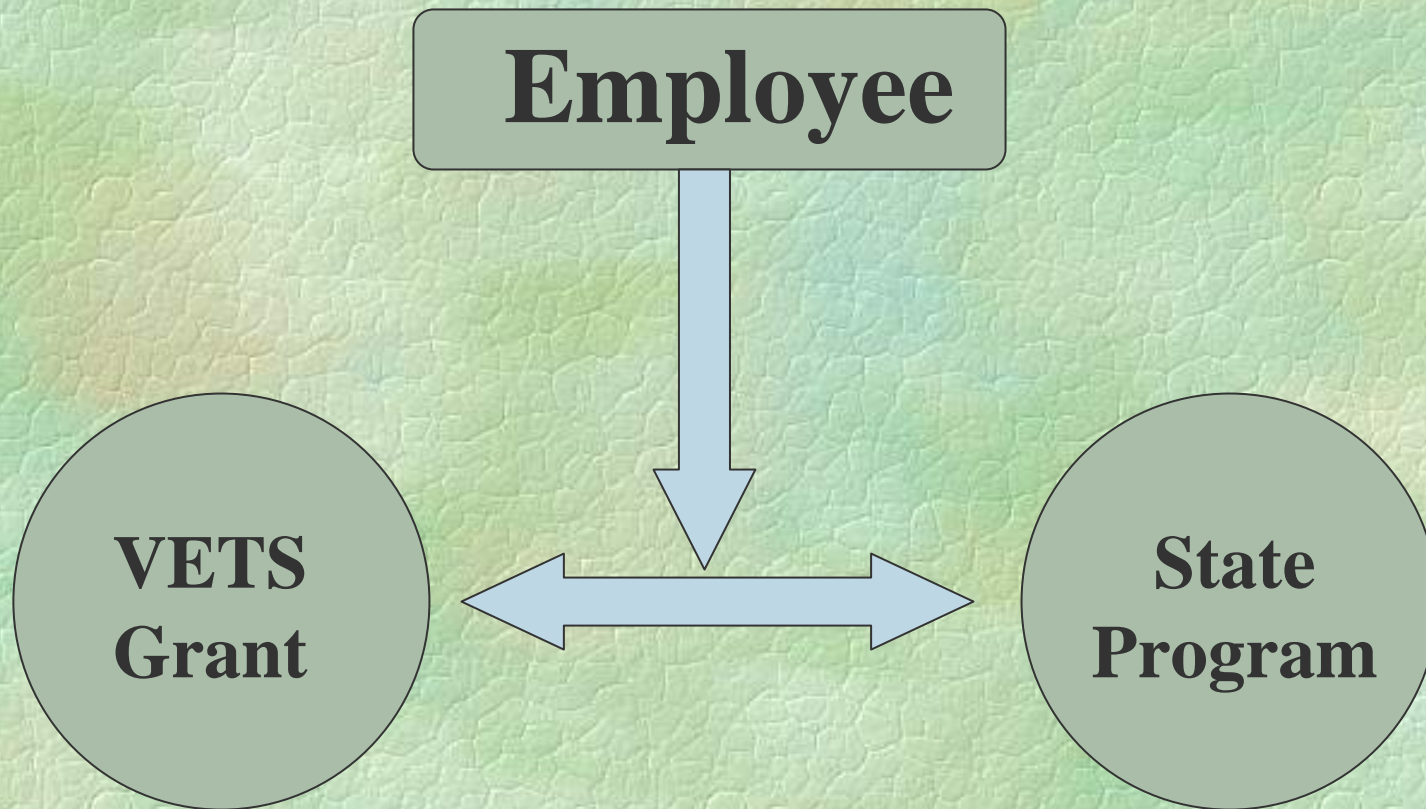
Compensation for Personnel Services(cont'd)

- PAR standards will apply where employees work on...

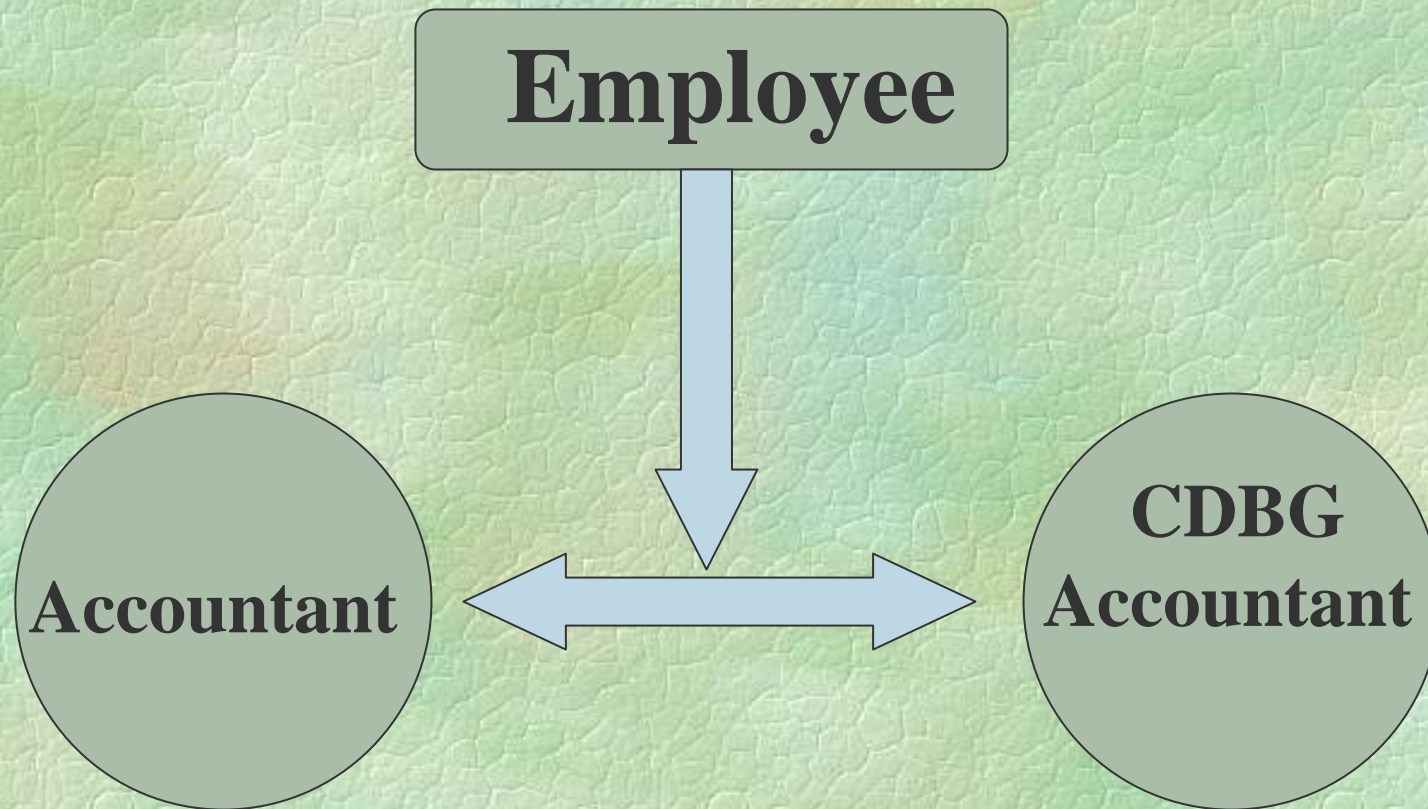
More than one Federal award



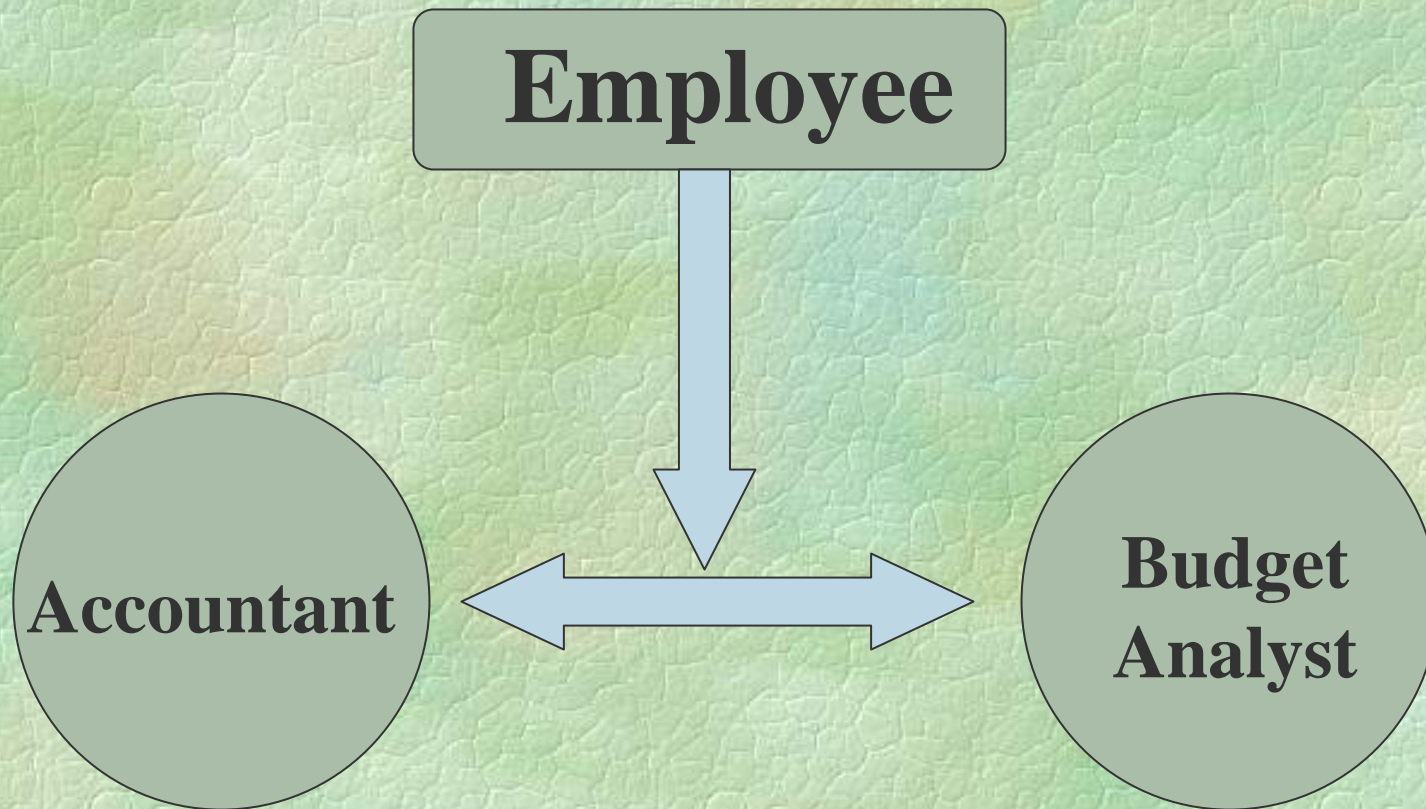
A Federal award and a non-Federal award



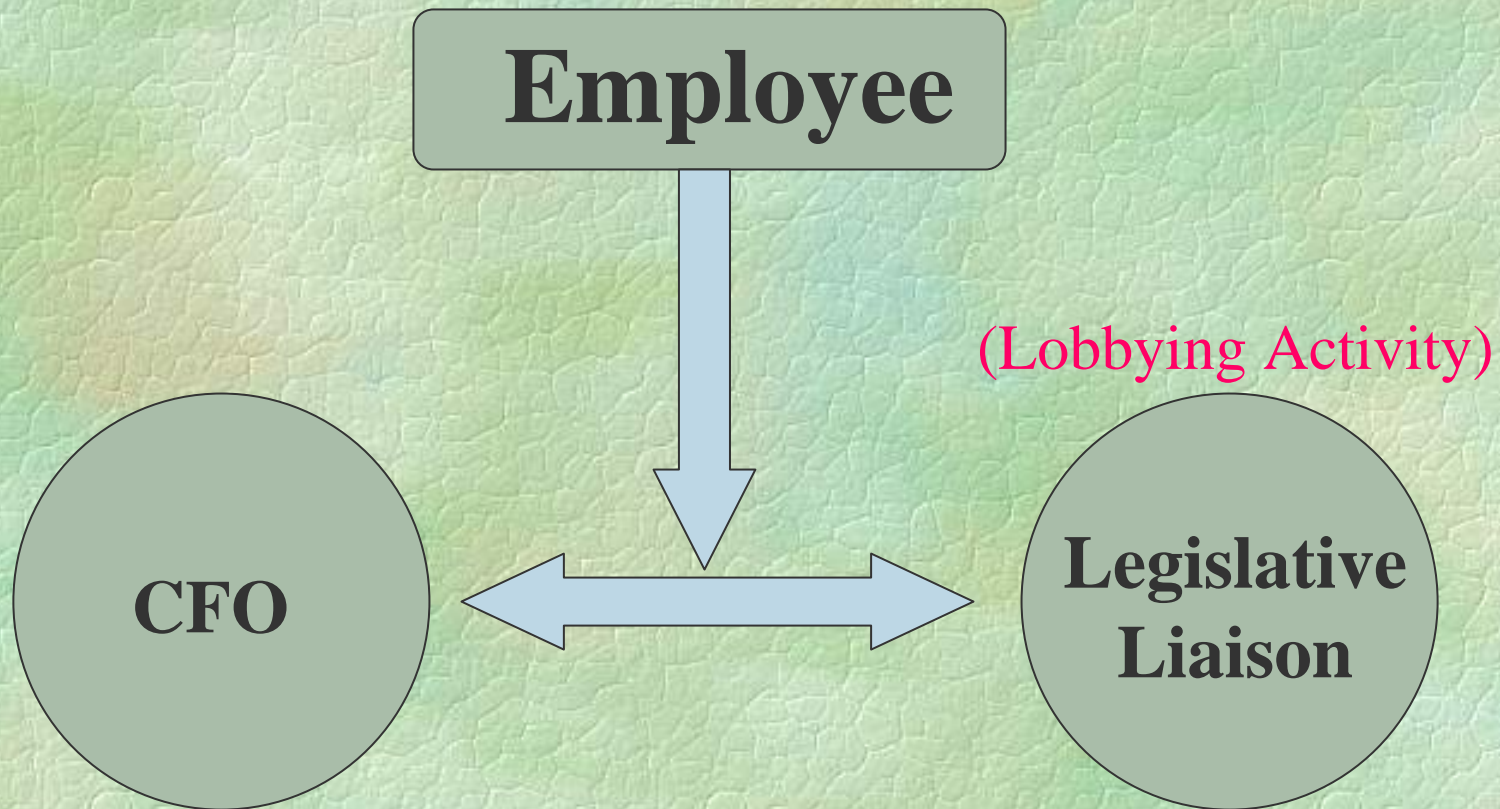
An indirect cost activity and a direct cost activity



Two or more indirect activities which are allocated using different allocation bases

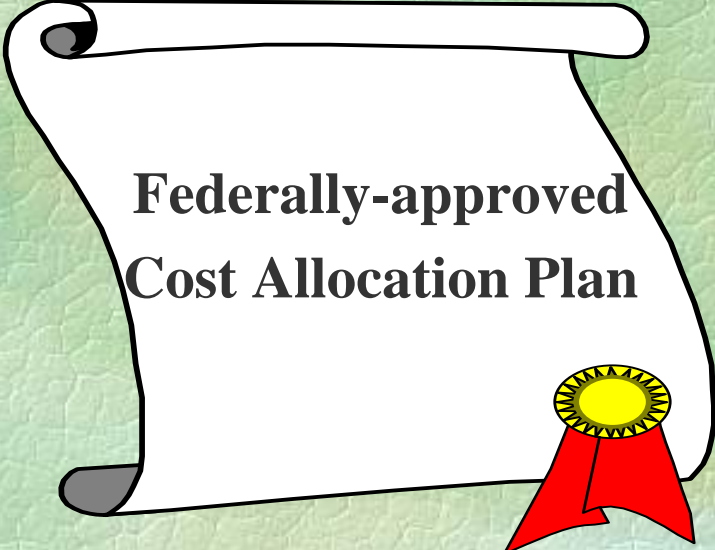


An unallowable activity and a direct or indirect cost activity



What is a Cost Allocation Plan?

- A document that identifies, accumulates, and distributes allowable direct and indirect costs and declares the allocation methods used for distribution.



**Federally-approved
Cost Allocation Plan**

Do not use the WAG Method to determine Indirect Costs!

Wild



Guess

What is an Indirect Cost Rate?

The ratio, expressed as a percentage, of an indirect cost pool and some direct cost base.

Some might say it's ...**PBR**...

Pabst
Blue Ribbon



How to compute an Indirect Cost Rate

$$\frac{\text{Pool (Pabst)}}{\text{Base (Blue)}} = \text{Rate (Ribbon)}$$

Indirect Cost Rate

- Example:

Indirect Cost Pool = \$ 10,000

Distribution Base = \$100,000

(Salaries & Benefits)

Indirect Cost Rate = 10%

What purposes are served by having the rate?

- Compliance with Federal regulations; e.g., OMB Circulars A-122, A-87 & A-21
- Management Information
- Documentation for auditors

Indirect Cost Rate

Examples of Allocation Bases

- Direct S/W including FB
- Direct S/W including release time, but excluding all other FB
- Modified Total Direct Cost(various)
 - Total Direct Costs excluding capital expenditures and flow-through funding

Indirect Cost Rates

Indirect Costs			<u>\$150,000</u>	
Direct Costs				
Salaries & Wages			\$300,000	
Other Direct Cost			<u>200,000</u>	
Total Direct Cost			<u>\$500,000</u>	
<u>\$150,000</u>				
\$300,000	=	50%	Direct Labor	
<u>\$150,000</u>				
\$500,000	=	30%	Total Direct Cost	

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Salaries	\$90,000
Fringe	30,000
Rent	10,000
Consultants	6,000
Travel	5,000
Supplies	3,000
Communications	2,000
Miscellaneous	<u>4,000</u>

Total Pool **\$150,000**

Base **\$300,000**
(direct SW+FB)

Rate **50%**

***Salaries & Benefits-directly identifiable
with a grant(s)**

Six Trainers	\$200,000
Three Counselors	100,000
Total Direct Sals & Bens	\$300,000

***Other Direct Costs-directly identifiable
with a grant(s)**

Occupancy	90,000
Travel	40,000
Participant Stipends	20,000
Participant Support Services	30,000
Supplies	10,000
Miscellaneous	<u>10,000</u>

Total Other Direct Cost \$200,000

Total Direct Sals & Bens	\$300,000
Total Other Direct Cost	<u>200,000</u>
Total Direct Cost Base	\$500,000
Total Indirect Cost Pool	\$150,000
Total Direct Cost Base	\$500,000
Rate	30%

\$Recovery of Costs\$

<u>Direct Labor Base</u>		<u>Total Direct Cost Base</u>	
Contract/Grant A	\$150,000	Contract/Grant A	\$275,000
- times rate	<u>50%</u>	- times rate	<u>30%</u>
Ind/Cost Recovery	\$75,000	Ind/Cost Recovery	\$82,500
Contract/Grant B	\$150,000	Contract/Grant B	\$225,000
- times rate	<u>50%</u>	- times rate	<u>30%</u>
Ind/Cost Recovery	\$75,000	Ind/Cost Recovery	\$67,500
Total Recovered	<u>\$150,000</u>	Total Recovered	<u>\$150,000</u>

	Total Costs	Unallowable Costs	Indirect Costs	Total Direct	DOL	All Other Funding Sources
	A=(B+C+D)	B	C	D=E+F	E	F
Salaries	\$589,000		\$70,000	\$519,000	\$219,000	\$300,000
Benefits	\$176,700		\$21,000	\$155,700	\$65,700	\$90,000
Other Costs	\$171,000	\$10,000	\$59,000	\$102,000	\$40,000	\$62,000
Total	\$936,700 *	\$10,000	\$150,000	\$776,700	\$324,700 a	\$452,000

Indirect Cost Rate Calculation/Distribution Using "Total Direct Salaries" as the Allocation Base

Indirect Costs	\$150,000				\$63,295 b	\$86,705
Total Direct Salaries	\$519,000					
Indirect Rate	28.9%					

Total Costs per Cost Center					\$387,995 a+b	\$538,705
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* Must reconcile to the Financial Statements.

Entity ABC
Statement of Total Costs
FYE 6/30/05

	Total Costs	Unallowable Costs	Indirect Costs	Total Direct	DOL	All Other Funding Sources
	A=(B+C+D)	B	C	D=E+F	E	F
Salaries	\$589,000		\$70,000	\$519,000	\$219,000	\$300,000
Benefits	\$176,700		\$21,000	\$155,700	\$65,700	\$90,000
Other Costs	\$171,000	\$10,000	\$59,000	\$102,000	\$40,000	\$62,000
Total	\$936,700 *	\$10,000	\$150,000	\$776,700	\$324,700 a	\$452,000

Indirect Cost Rate Calculation/Distribution Using "Total Direct Costs" as the Allocation Base

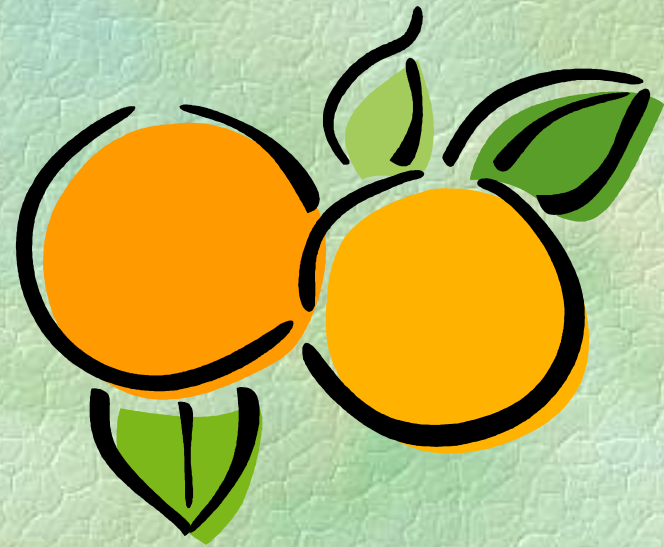
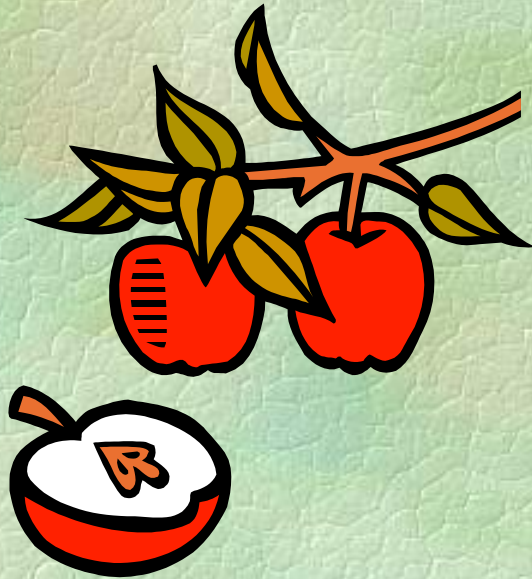
Indirect Costs	\$150,000				\$62,708 b	
Total Direct Costs	\$776,700					
Indirect Rate	19.3%					

Total Costs per Cost Center					\$387,408 a+b	\$539,292
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* Must reconcile to the Financial Statements.

Cost Allocation versus Cost Reimbursement Two Separate Concepts...



Cost Allocation

- Cost allocation is the measurement of allowable costs that are then allocated based on benefits received by each program/agency.
- Use A-122, A-87, A-21 guidelines in the cost allocation process.
- The cost principles provide the guidance for determining a Federal program's share of both direct and indirect costs. They have no authority over the actual payment of the costs. The payment is governed by the terms of the grant document or the legislation authorizing the program.

Cost Reimbursement

- Cost reimbursement is the process where Federal dollars are used to reimburse grantee organizations for allowable costs.
- Use grant language/cost limitations and legislative constraints as guidelines in the payment process.

Methods of Calculation

- Simplified Method
 - Federal awards are not material
 - Organization has only a single function
 - All programs benefit from indirect costs to about the same degree

Simplified Method

Central Services

Personnel
Accounting
Purchasing

Departmental Admin

Director's Office
Space
Supplies

DOL Programs

HHS Programs

S/L Programs

**Allocation Base
Salaries & Wages**

Methods of Calculation

- Multiple Allocation Base
 - All programs do not benefit to the same degree
 - Indirect costs are pooled and allocated to direct cost objectives based on various distribution bases (for example, # of transactions, # of purchase orders, # of FTE's)
 - Primarily used by A-87 organizations that capture costs by department or division (for example, accounting, purchasing, personnel, etc.)

Multiple Allocation Base Method

Central Services

Personnel - # FTEs

Purchasing - # POs

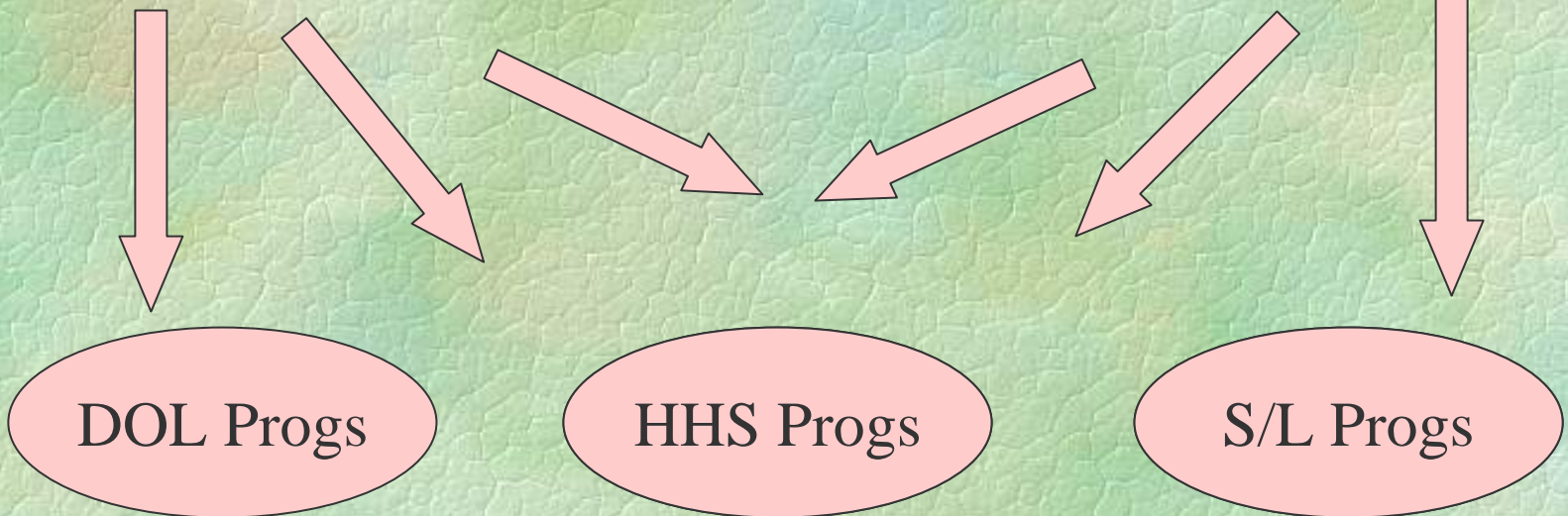
Accounting - #Trans

Dept Admin

Dir Office - S/W

Space - Square Ft

Supplies - Usage

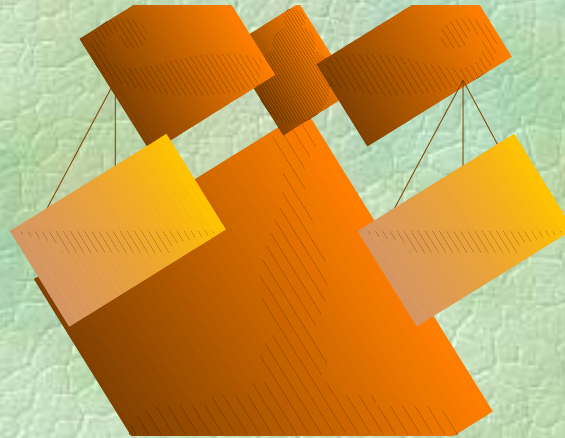


Methods of Calculation

- Direct Allocation Method
 - All costs are charged directly to programs to except for general administration
 - Preferred method used by a majority of nonprofit organizations
 - Various bases are selected to “directly allocate” costs to programs(for example, space allocated based on square footage occupied)
 - See DCD website for guide to this method

Allocation of Costs

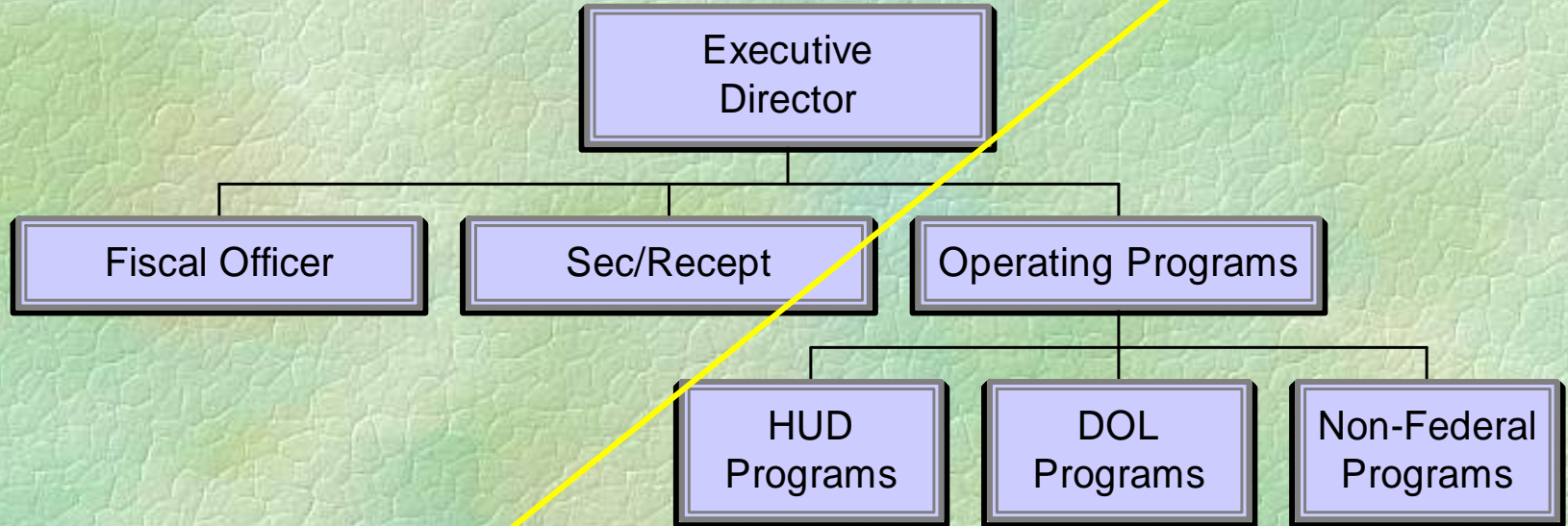
- Any method of distribution can be used if it results in an equitable distribution of costs based on “benefits received”.



What's Allocable?

Pool

Typical Nonprofit Corporation, Inc.



Base

Direct vs. Indirect Costs

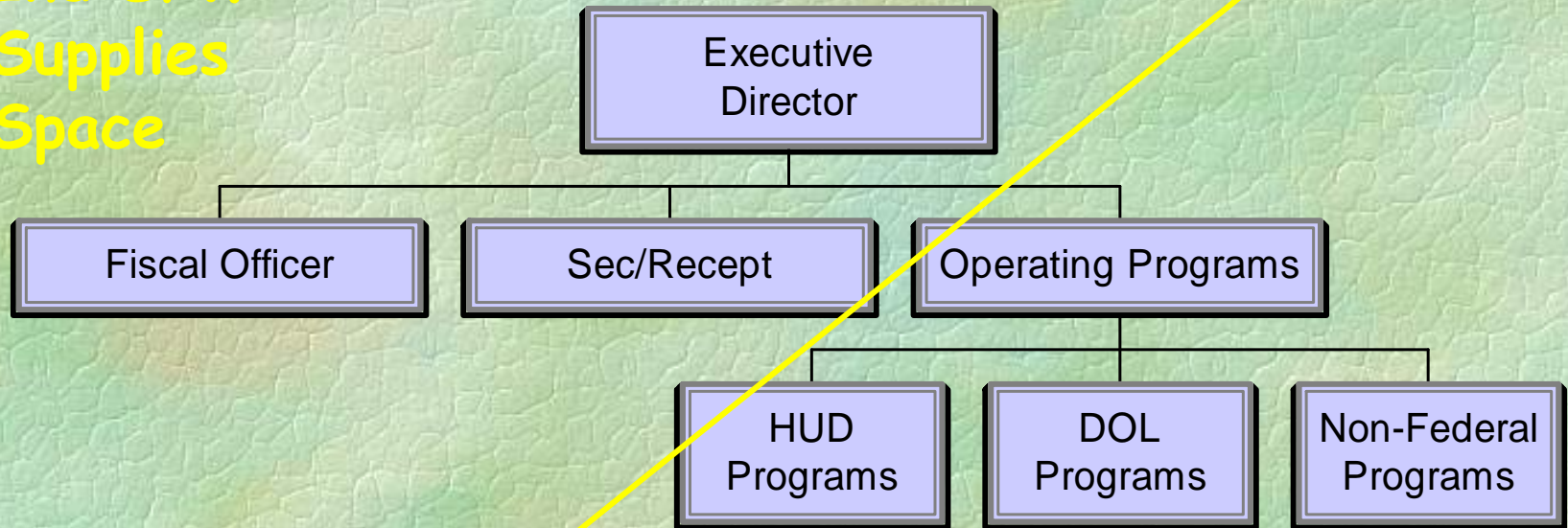
- The decision to treat a cost as either a direct cost or an indirect costs depends upon the treatment of that cost within the grantee's accounting system.
- Cost Policy Statements (CPS) provide documentation on how the grantee treats costs within the accounting system.



Direct vs. Indirect Costs

Typical Nonprofit Corporation, Inc.

Ind S/W
Supplies
Space



Program S/W
Supplies
Space

Are administrative costs and indirect costs one in the same? No!

Allocation versus Classification

- Allocation involves assigning costs to the benefiting objective(s) equitably. This process is covered by A-87, A-122 and other cost principles.
- Classification of costs involves placing costs into some category such as administration, program, or some other category as prescribed by statute.

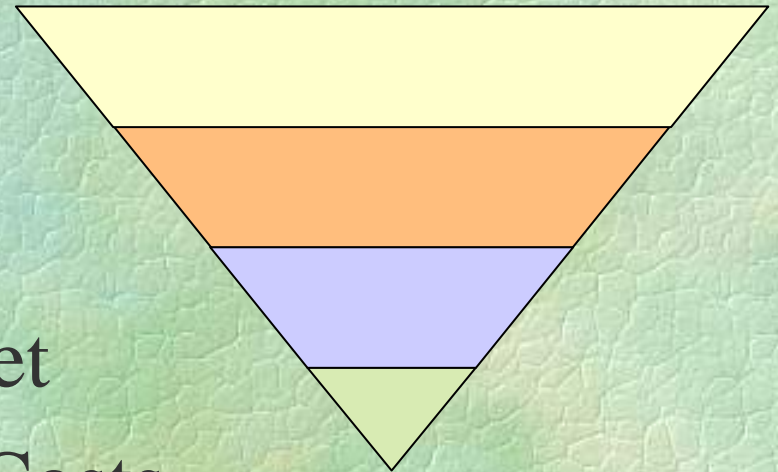
Submission of Indirect Cost Rate Proposals



- Proposals must be submitted annually
 - No later than six months after the end of the organization's fiscal year
 - New grantees must submit within three months after the effective date of the award
 - Extensions of time may be granted

Submission of Indirect Cost Rate Proposals

- Organizational Chart
- Cost Policy Statement
- Financial Reports
- Personnel Cost Worksheet
- Allocation of Personnel Costs



(continued)

Submission of Indirect Cost Rate Proposals

- Statement of Employee Benefits
- Indirect Cost Rate Proposal(s) reconciled with the financial reports, audit report or budget
- A completed Certificate of Indirect Costs (must be signed and dated!)
- A listing of grants and contracts showing source, amounts, and relevant dates

Indirect Cost Clause (in DOL grants)

Clause #2: - INDIRECT COST RATE AND COST ALLOCATION PLAN

This clause is applicable to all awardees receiving funds from multiple sources. Organizations receiving funds from only one source do not need an indirect cost rate (ICR) approved or cost allocation plan (CAP).

Mark the appropriate clause for your organization and fill in the blanks, as appropriate:

_____ A. A current approved CAP or ICR agreement dated _____ has been provided and approved by _____ (Federal Cognizant agency - *Copy Attached*).

Regarding only the ICR agreement, please provide the following:

a) Indirect Rate approved _____ %.

b) Type of Indirect Cost Rate (Provisional/Fixed) _____.

c) Allocation Base _____.

d) Current period applicable to rate _____.



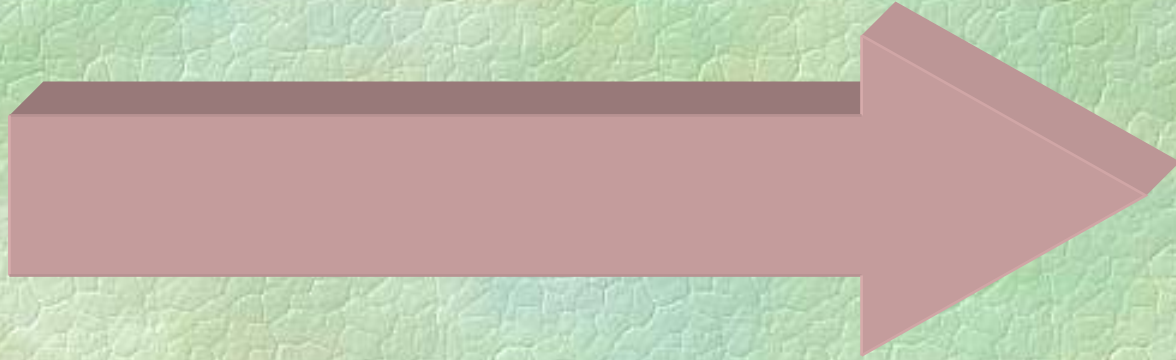
Indirect Cost Clause, cont.

- _____ B. No CAP or ICR agreement has been approved by a Federal Agency.
- **Note:** Regarding “B”, a Temporary Billing Rate of _____% has been approved
- by _____ [(grant/contracting officer
- at the Departmental agency (Example: ETA)] for the first **90 days** of the grant
- period. This rate is based on the fact that your organization has not established _____ an ICR agreement or approved CAP.
- Within this 90-day period, you must submit an acceptable indirect cost proposal or CAP to your Federal cognizant agency (1) to obtain a provisional indirect rate or a CAP approved. ***Failure on your part to submit an indirect cost proposal within this 90 day period means that you shall not receive further reimbursement for your billing rate.***
- If DOL is your Federal cognizant agency, proposals shall be sent to the appropriate office in the DOL’s Division of Cost Determination (see detailed list attached).
- (1) Providing preponderance of Federal funds to the organization.

Indirect Cost Clause, cont.

- **Ceiling Indirect Rates or Ceiling Amounts (applicable to A or B above):**
- An Indirect Cost ceiling either in the amount of \$_____, or a rate of _____%, based on _____, as the indirect cost allocation base (1) has been applied under this agreement based on the grantee's budget and written documentation received.
- The total amount of DOL's financial obligation under this award *will not be* increased to reimburse awardee organizations for higher negotiated indirect cost rates than those rates identified in this clause.
- **Note:**
- A ceiling rate or dollar amount does not exclude your organization from the responsibility of submitting an indirect cost rate for approval.
- (1) For example: direct salaries, direct salaries and fringes, total direct costs, etc.

Types of Indirect Cost Rates



Hmmm?

- Billing
- Ceiling
- Provisional
- Final
- Fixed
- Predetermined



Billing Rate

- Rate stated in the award to allow recovery of indirect costs until an indirect cost proposal is completed and submitted.
- Normally only valid for 90 days.

Ceiling Rate

- Set by the Contract/Grant Officer
- The maximum rate at which indirect costs may be recovered under a particular award

Provisional Rate

- A rate based on projected information, historical information, or a combination of the two for the organization's fiscal year
- This rate allows for recovery of indirect costs during the contract/grant period until the rate can be finalized

Final Rate

- The experienced indirect cost rate based on actual data for the organization's fiscal year
- All provisional indirect cost rates must eventually be “finalized”

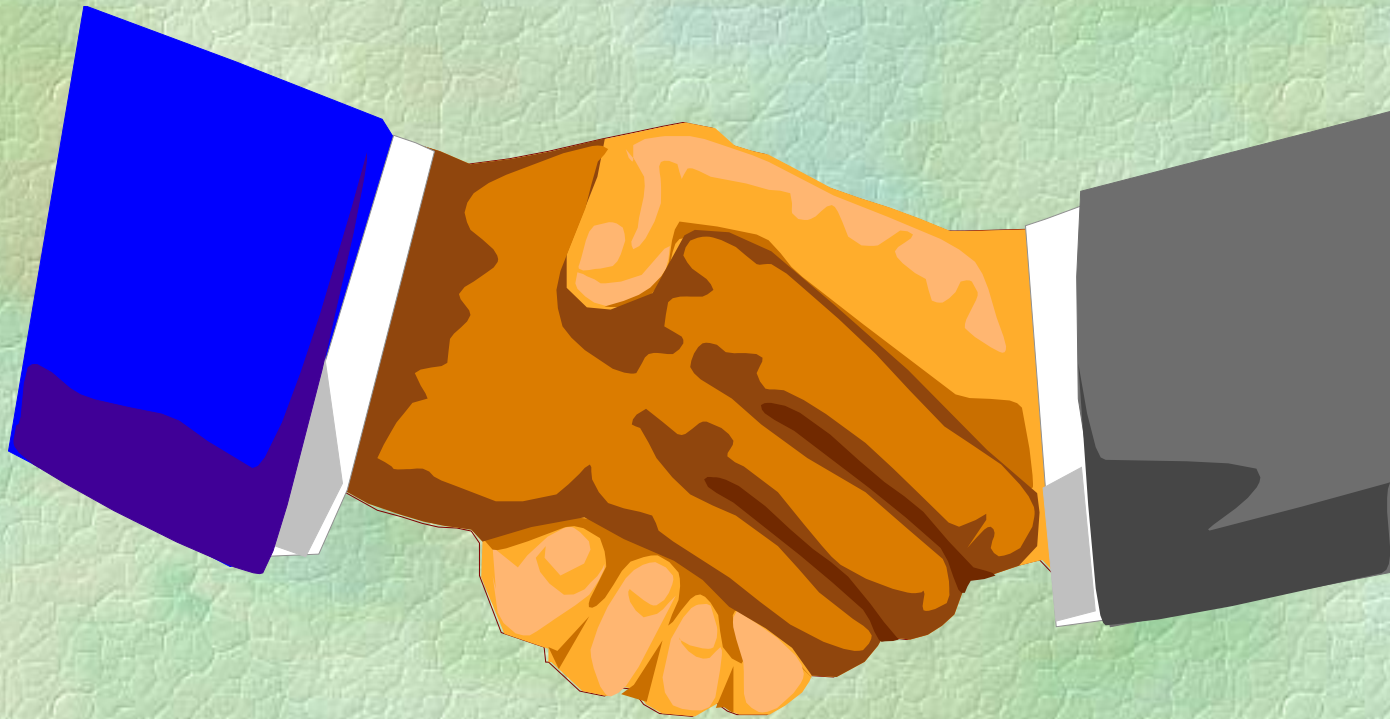
Fixed Rate

- A permanent rate that is not subject to change
- Any differences between estimated and actual costs are carried forward as adjustments to rate computations in future periods
- Seldom issued to nonprofit organizations

Predetermined Rate

- A rate negotiated for a certain length of time, usually several years
- Not subject to change

Example of an Indirect Cost Rate Agreement



(An Example)
INDIRECT COST NEGOTIATION AGREEMENT
NONPROFIT ORGANIZATION

ORGANIZATION:
XYZ Nonprofit Agency, Inc.
Podunk, AL 99999-9999

DATE: December 1, 2004
FILE REF: This replaces the
negotiation agreement dated
October 12, 2003

The indirect cost rate(s) contained herein are for use on grants and contracts with the Federal Government to which OMB Circular A-122 applies subject to the limitations contained in the Circular and Section II-A, below. The rate(s) were negotiated by XYZ Nonprofit Agency, Inc. and the U. S. Department of Labor in accordance with the authority contained in Attachment A, Section E, of the Circular.

The indirect cost rate(s) contained herein are for use on grants and contracts with the Federal Government to which OMB Circular A-122 applies subject to the limitations contained in the Circular and Section II-A, below. The rate(s) were negotiated by XYZ Nonprofit Agency, Inc. and the U. S. Department of Labor in accordance with the authority contained in Attachment A, Section E, of the Circular.

<u>Type</u>	<u>Effective Period</u>		<u>Rate</u>	<u>Location</u>	<u>Applicable to</u>
	<u>From</u>	<u>To</u>			
Final	7/1/02	6/30/03	14.25%	All	All Programs
Final	7/1/03	6/30/04	15.25%	All	All Programs
Provisional	7/1/04	6/30/05	17.17%	All	All Programs
Provisional	7/1/05	6/30/06	16.43%	All	All Programs
		<i>(See Special Remarks)</i>			

BASE*:

Total direct salaries and wages including vacation, holiday and sick pay but excluding all other fringe benefits.

TREATMENT OF FRINGE BENEFITS:

Fringe benefits are specifically identified to each employee and are charged individually as direct costs. The directly claimed fringe benefits are listed in the Special Remarks Section of this Agreement.

TREATMENT OF PAID ABSENCES:

Vacation, holiday, sick leave and other paid absences are included in salaries and wages and are claimed on grants, contracts and other agreements as part of the normal cost for salaries and wages. Separate claims for these absences are not made.

A. LIMITATIONS: Use of the rate(s) contained in this Agreement is subject to any statutory or administrative limitations and is applicable to a given grant or contract only to the extent that funds are available. Acceptance of the rate(s) agreed to herein is predicated upon the following conditions:

- (1) that no costs other than those incurred by the grantee/contractor or allocated to the grantee/contractor via an approved central service cost allocation plan were included in its indirect cost pool as finally accepted and that such incurred costs are legal obligations of the grantee/contractor and allowable under the governing cost principles,
- (2) that the same costs that have been treated as indirect costs have not been claimed as direct costs,
- (3) that similar types of costs have been accorded consistent treatment, and
- (4) that the information provided by the grantee/contractor which was used as a basis for acceptance of the rate(s) agreed to herein is not subsequently found to be materially inaccurate.

The elements of indirect cost and the type of distribution base(s) used in computing provisional rates are subject to revision when final rates are negotiated. Also, the rates cited in this Agreement are subject to audit.

B. CHANGES: The grantee/contractor is required to provide written notification to the indirect cost negotiator prior to implementing any changes which could affect the applicability of the approved rates. Changes in the indirect cost recovery plan, which may result from changes such as the method of accounting or organizational structure, require the prior written approval of the Division of Cost Determination (DCD). Failure to obtain such approval may result in subsequent cost disallowance.

C. NOTIFICATION TO FEDERAL AGENCIES: A copy of this document is to be provided by this organization to other Federal funding sources as a means of notifying them of the Agreement contained herein.

D. PROVISIONAL-FINAL RATES: The grantee/contractor must submit a proposal to establish a final rate within six months after their fiscal year end. Billings and charges to Federal awards must be adjusted if the final rate varies from the provisional rate. If the final rate is greater than the provisional rate and there are no funds available to cover the additional indirect costs, the organization may not recover all indirect costs. Conversely, if the final rate is less than the provisional rate, the organization will be required to pay back the difference to the funding agency.

Indirect costs allocable to a particular award or other cost objective may not be shifted to other Federal awards to overcome funding deficiencies, or to avoid restrictions imposed by law or by the terms of the award.

E. SPECIAL REMARKS:

1. Indirect costs charged to Federal grants/contracts by means other than the rate(s) cited in this Agreement should be adjusted to the applicable rate cited herein and applied to the appropriate base to identify the proper amount of indirect costs allocable to the program.

2. Grants/contracts providing for ceilings as to the indirect cost rates(s) or amount(s) which are indicated in Section I above, will be subject to the ceilings stipulated in the contract or grant agreements. The ceiling rate or the rate(s) cited in this Agreement, whichever is lower, will be used to determine the maximum allowable indirect cost on the grant or contract agreement.

3. Fringe benefits other than paid absences consist of:
- | | |
|---------------------------|--------------|
| Worker's Compensation | FICA |
| Health Insurance | Pension Plan |
| Unemployment Compensation | |

4. XYZ Nonprofit Agency, Inc. staff maintain 100% time distribution records. The indirect cost pool consists of:
- a) Salaries and fringe benefits of the following positions:
- | | |
|--------------------|--------------------|
| Executive Director | Dir of Fiscal Svcs |
| Account Tech II | Admin Secretary |
- b) Support costs of the above positions as follows:
- | | |
|-----------------------|-----------------------|
| Professional Services | Travel |
| Space | Supplies |
| Equipment Leases | Insurance & Bonding |
| Publications & Dues | Repairs & Maintenance |
| Communications | Postage |
| Miscellaneous | |

ACCEPTANCE

BY THE ORGANIZATION:

**BY THE COGNIZANT AGENCY
ON BEHALF OF THE FED GOV:**

XYZ Nonprofit Agency, Inc.

U. S. Department of Labor

(Organization)

(Agency)

(Signature)

(Signature)

Jane Doe

Jack B. Nimble

(Name)

(Name)

Executive Director

Chief, Division of Cost Determination

(Title)

(Title)

December 1, 2004

December 1, 2004

(Date)

(Date)

USDOL Negotiator: Phil Zahnd

Telephone No.: 256.272.0075

Questions?

