

# Presenter Information

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# Our Topics for This discussion:

To provide an overview of the following as it pertains to IDC and tribal Nations

- Cost allocation
- Public Law 93-638 as it relates to Contract Support
- Direct Costs
- Indirect Costs
- Allowable costs
- Allocable costs
- Reasonable costs
- Cost Allocation Plans
- IDC Rates
- The process for charging IDC to a grant

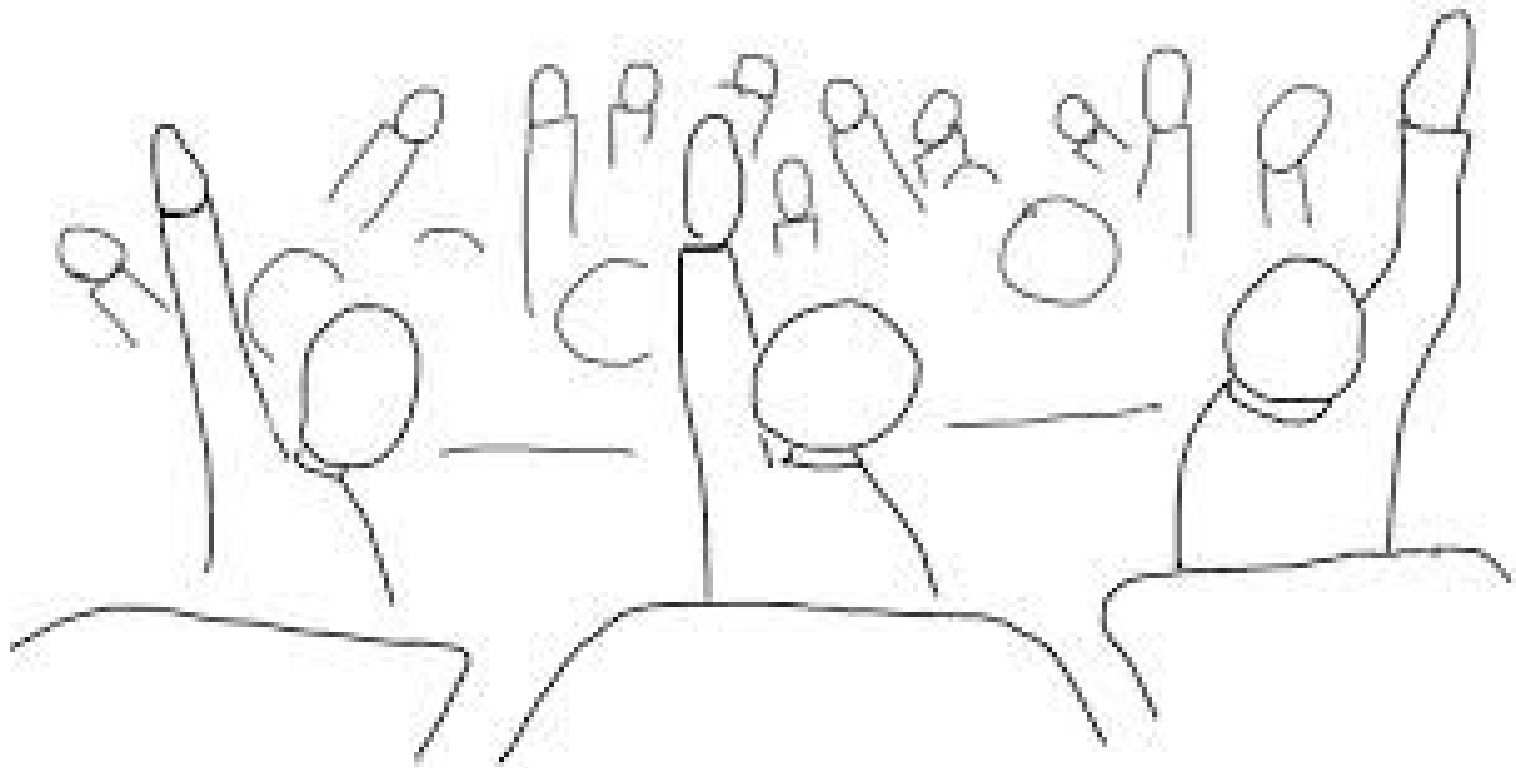


- The process for budgeting for IDC for a program
- Factors to consider before accepting a grant
- The Federal rules governing the IDC process
- The 2 major court cases impacting IDC
- The 7 steps for preparing an IDC Proposal
- Common problems that auditors find with IDC

# Key Points or Goals

1. Understand the Costs and what it takes to execute on the mission of the program
2. How different types of Costs effect my program (benefits derived)
3. Where do those Costs originate and how are they determined

Don't be afraid to ask questions. The more involved you are, the more we all learn!



# True Cost of Labor

Salary	\$40,000
Fringe @ 30% of Salary	\$12,000
Supplies, computer, etc.	\$2,500
<u>Direct Costs</u>	<u>\$54,500</u>
<i>Indirect Costs @ 25% of Direct</i>	<i>13,625</i>
<b>Total Costs</b>	<b>\$68,125</b>

Note: Using Modified Total Direct to calculate IDC

All Costs must be  
Allowable, Allocable, and Reasonable?  
What does that mean?

Allowable



Reasonable

Allocable

# To be Allowable, costs must:

- **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 (in accounting system and over time)**
- **Be determined in accordance with GAAP**
- **Not already be included in a cost sharing or matching requirement**

Continued...

# More Tests for Allowability

- Is it unallowable by law/resolution/or grant or contract agreement?
  - Read your agreements carefully!
- Is it net of all applicable credits?
- Is it adequately documented?





# Reasonable Cost

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.



# In Determining Reasonableness of a Cost, Consideration Must Be Given To:

- Whether the cost is of a type generally recognized as ordinary and necessary for the operation of the organization or the performance of the award.
- Market prices for comparable goods or services.



# In Determining Reasonableness of a Cost, Consideration Must Be Given To:

The restraints or requirements imposed by such factors as:

- sound business practices;
- arms length bargaining;
- laws and regulations; and
- terms and conditions of the award.



# In Determining Reasonableness of a Cost, Consideration Must Be Given To:

- Significant deviations from the established practices of the Tribe which may unjustifiably increase the award's cost.



# In Determining Reasonableness of a Cost, Consideration Must Be Given To:

- Whether the individuals concerned acted with prudence in the circumstances considering their responsibilities to the Tribe, its employees, the public at large, and the federal or state government.



# Allocable Costs (see ASMB C-10, 2.8.2)

Cost is **allocable** to a particular cost objective if the goods or services involved are *chargeable or assignable* to such cost objective *in accordance with the relative benefits received*.

- Applies whether the cost is direct or indirect.
- Shifting of costs between awards to overcome funding deficiencies is not allowed




- (a) Is incurred specifically for the contract;
- (b) Benefits both the contract and other work, and can be distributed to them in reasonable proportion to the benefits received; or
- (c) Is necessary to the overall operation of the business, although a direct relationship to any particular cost objective cannot be shown.

# Allocable Costs

For a cost to be allocable to a Federal award it must be treated consistently with other costs incurred for the same purpose in like circumstances



What are  
Direct and  
Indirect  \$  
Costs?



# What are “Direct Costs”?

**Direct costs** are those costs that can be identified specifically with a particular sponsored project or activity, or that can be directly assigned to such activities relatively easily with a high degree of accuracy.

- The vast majority of costs are **direct** costs.



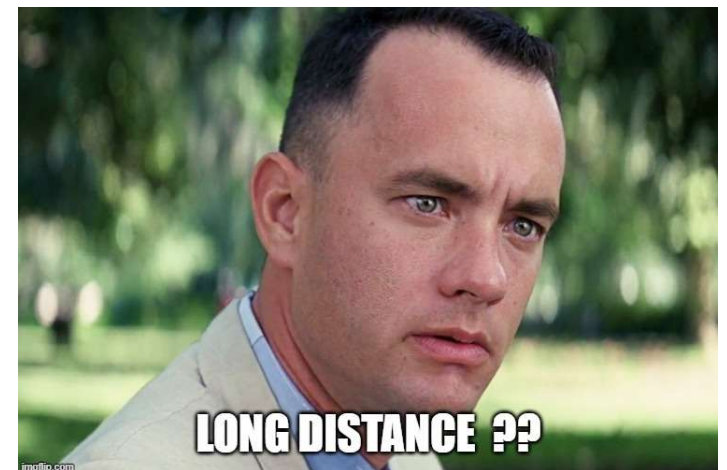
# Examples of Typical Direct Costs

- **Program** salaries and wages (including vacations, holidays, sick leave, and other excused absences of employees working specifically on objectives of a grant or contract – i.e., direct labor costs).
- Other employee fringe benefits allocable on **direct labor** employees.
- Consultant services contracted **to accomplish specific grant/contract objectives.**



# Examples of Typical Direct Costs

- Travel costs for **program** activities.
- Materials, supplies and equipment **purchased directly for use on a specific grant or contract.**
- Communication costs, such as long distance telephone calls or telegrams **identifiable with a specific award or activity.**



# What's Another Way of Explaining What a Direct Cost is?

- Anything that isn't an Indirect Cost
- So, what's an Indirect Cost, then?



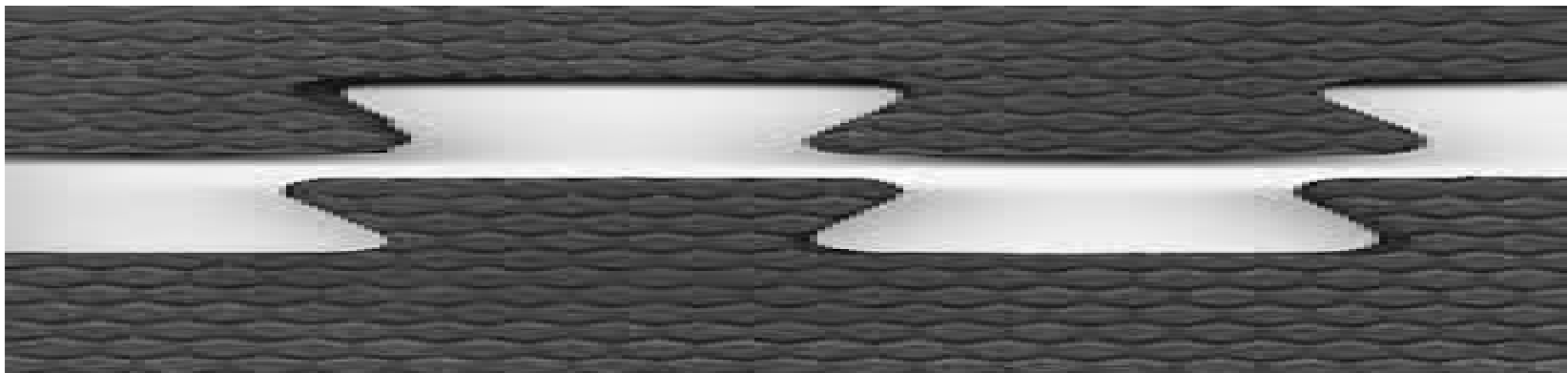
# What's an Indirect Cost?

- Anything that isn't a Direct Cost



# Indirect Costs

- After direct costs have been determined and assigned directly to Federal awards and other activities as appropriate, indirect costs are those remaining to be allocated to benefited cost objectives.



# Examples of Indirect Costs

## Specific Examples:

- rent
- utilities
- Development, IT, Finance, salaries
- supplies that aren't specifically related to programs, but benefit all programs
- communications costs that benefit all programs
- **OMB does not define what is and is not a Direct or Indirect Cost \*\*\* They just can't be treated as both**

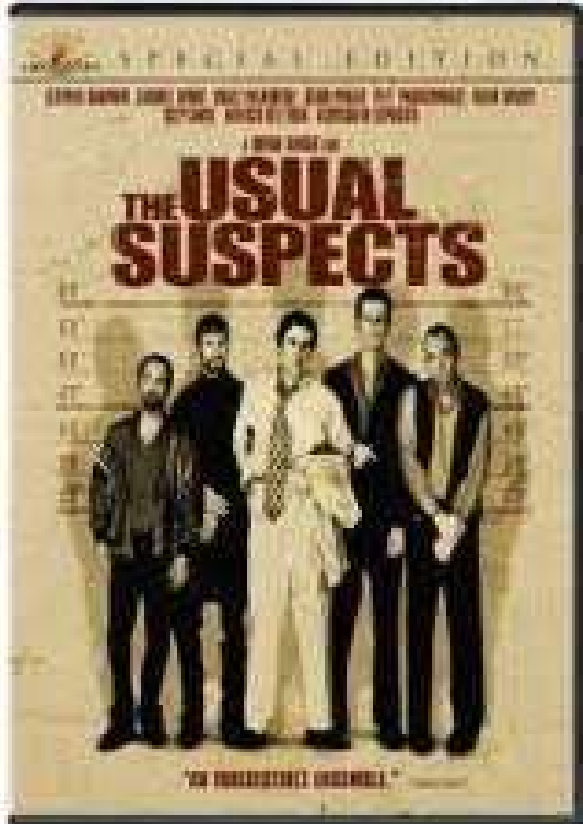


# Indirect Costs

- Indirect costs are costs that are incurred to provide **administrative support to all programs**, and are **not readily identifiable with a specific federal grant, contract, project function, or activity**



# Most Common Indirect Costs:



**Management and Administration:** Governing Body, Management and Planning, Financial Management, HR Management, Property Management, Records Management, Data Processing, Office Services

# Most Common Indirect Costs:



**Facilities and Equipment:** Building  
Rent/Lease/Cost Recovery, Utilities, Janitorial,  
Building and Grounds, Maintenance, Equipment  
Equipment

# Most Common Indirect Costs:

**General Services and Expenses:** Insurance and Bonding, Legal Services, Audit, General Support Services



# Allocating Costs

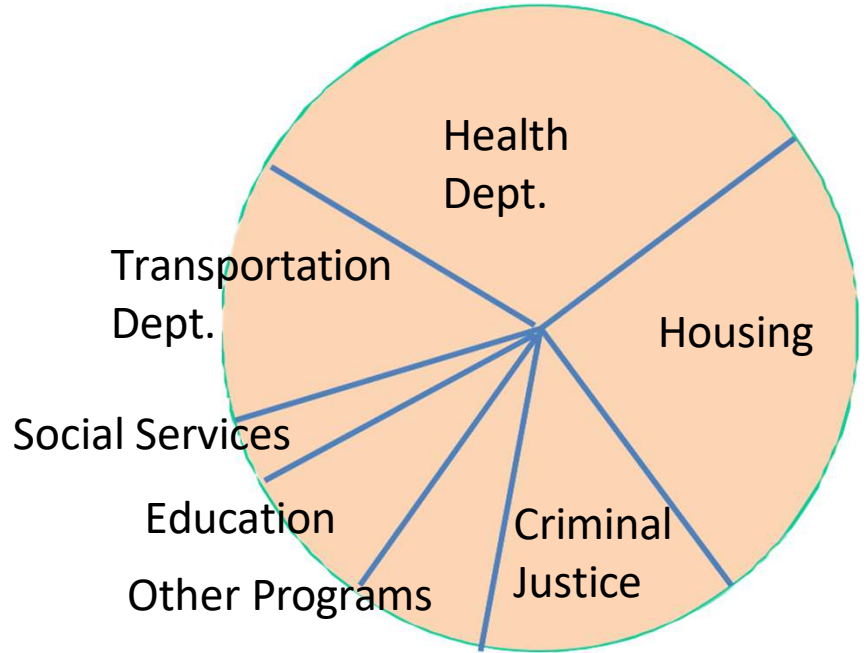
- We use the process of **cost allocation** to assign common/shared resource costs to cost objectives (programs, activities, etc.) without arbitrary appointment.
- Done through dividing a pool of costs and assigning to programs, activities, etc.
- An effective cost allocation methodology enables an organization to identify what services are being provided and what they cost, to allocate costs to programs, and to manage cost recovery.

# Why is Cost Allocation Important?

- Finds the true cost of a product or service
- Helps identify financially untenable programs
- Helps senior management/tribal council make more informed strategic and financial decisions
- Calculates the true amount of funding needed to cover all the costs of a program.



- OMB Uniform Guidance at 2 CFR part 200 require all activities which **benefit from the governmental unit's indirect costs to receive an appropriate allocation of indirect costs.**



**Benefits Received  
from IDC**

=



**Responsibility for  
Paying for IDC**

# How do we allocate costs that aren't easily traceable?





# Cost Allocation Overview

- **Simple Example:**
  - **Centrally Located Copier**
    - **“Cost to Operate” includes:**
      - Lease Payments
      - Repairs & Maintenance
      - Toner
      - Paper

# Cost Allocation Overview

- **Copier Example  
(continued):**
  - **Three Divisions Utilize**
    - **Division A – 12 Staff**
    - **Division B – 6 Staff**
    - **Division C – 22 Staff**

# Cost Allocation Overview

- **Copier Example (continued):**
  - **How Do We Apportion or Allocate These “Costs” to the Three Divisions?**
    - **Equal Distribution (i.e., 1/3rd Each)**
      - “Good”
    - **Number of Staff Using the Copier**
      - A – 30%, B – 20%, C – 50%
      - “Better”
    - **User Codes**
      - **Measures Actual Usage of the Copier**
      - “Best”

# How are Indirect Costs Charged to Federal Awards?

Reimbursed According To:

- Indirect Cost Rate; or
- “Indirect Type Costs”
  - For awardees without a negotiated IDC Rate or one that’s 4 years old or older.
  - A lump sum amount may be computed (lump sum agreement negotiated)
  - **Not sure if this is still the case with many awards**



“The most important thing about Direct Costs is...”  
“The most important thing about Indirect Costs is...”  
4 Things



- The term “indirect cost” is a bit of a misnomer—programs actually directly use “indirect” services like heat, light, accounting, and personnel--it’s just that these costs aren’t easily traceable.

If all costs are theoretically directly attributable given the right measurement, how does your Tribe or org determine what’s classified as an IDC?



# Finance Makes the Decision

- Direct Costs are spelled out in the budget explicitly
- Will be different depending on the size of the Tribal Nation



# Note on Consistency

- A cost may not be allocated to a Federal award as an *indirect* cost if any other cost incurred for the same purpose, in like circumstances, has been assigned to a Federal award as a *direct* cost.
- Once a grantee makes an election and treats a given cost as direct or indirect, that treatment must be applied consistently and may not change during the fiscal year.





What Do **You** Think?

Fringe Benefits – Direct or  
Indirect?

# Fringe Benefits – Direct or Indirect?

- If the position is classified as a direct position, then the salary - along with applicable fringe benefits - should also be treated as direct costs.
- If the position is classified as an indirect position, then the related fringe benefits are to be treated as indirect costs.

# Discussion

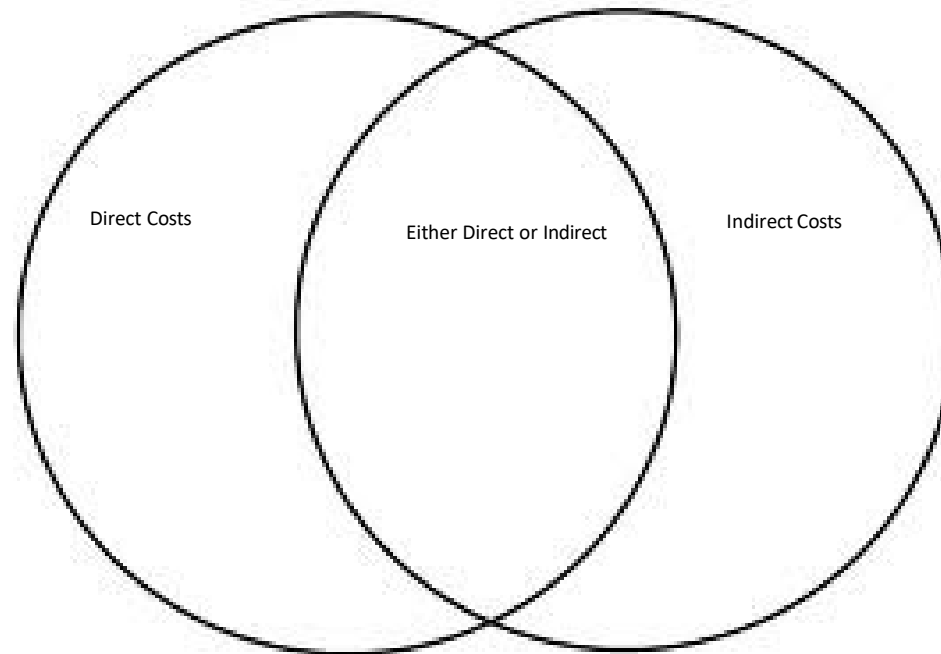
Is it always clear-cut if a cost is direct or indirect?

What are some of the factors that should be considered when deciding if a cost is direct or indirect?

Do you think a Program Director's salary should be a direct or indirect cost? What about an Executive Director?

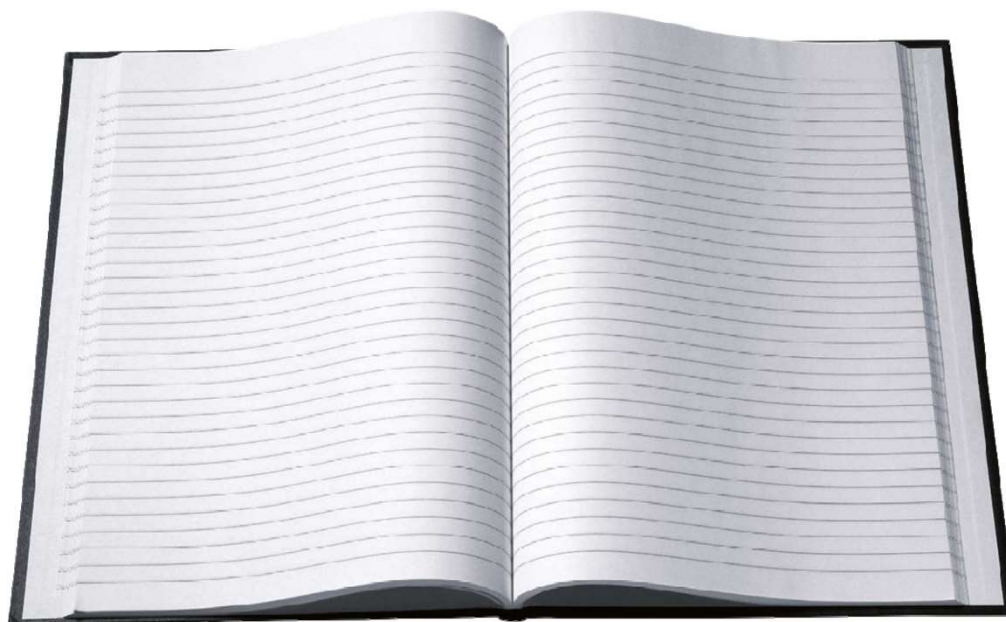


# Exercise: Using a Venn Diagram to Chart Direct vs. Indirect Costs





# More Terms You Should Know





## Indirect Cost Rate

- An indirect cost rate is a tool for determining the proportion of indirect costs each program should bear. It's the methodology used to allocate administrative costs to programs.



## Indirect Cost Rate

- The ratio (expressed as a percentage) of the pooled indirect costs of an organization to a base of its direct costs.
- Negotiation of the Rate involves a detailed budget proposal for the IDC Pool  
(More in-depth discussion later)



What's the Formula for an Indirect Cost Rate?

$$\frac{\textit{Pooled Indirect Costs}}{\textit{Base of Direct Costs}} = \textit{Rate}$$

Or to put it more simply:

$$\frac{\textit{Pool}}{\textit{Base}} = \textit{Rate}$$

# **Indirect Cost Rate Example Calculation**

**Indirect Cost Pool  
Divided by  
Direct Cost Base**

**Indirect Cost Pool = \$2,000,000**

**Direct Cost Base = \$6,000,000**

**Rate = 33%**

# Indirect Cost Pool (“The Pool”)

All the Indirect Costs of the Tribe together make up the pool.

- The pool is accumulated costs that jointly benefit two or more programs or other cost objectives.
- The pool is used as the numerator of the Indirect Cost Rate formula



# Indirect Cost Pool

- Administrative cost center for your organization.
- AKA Internal Service Fund.
  - NOT same as General Fund
- Costs charged to IDC Pool must be allowable charges to federal grants & contracts.

# Indirect Cost Pool

- Allocated to programs according to an *Indirect Cost Rate Agreement*.
- Tribal governments are required to negotiate a rate agreement each year in order to recover administrative costs from federal grants and contracts.
  - Or now can negotiate one for 4 years

# IDC Pool Usually Includes

- Executive Administration (portion of time spent in direct support of programs)
- Programs Administrator
- Finance Department
- Human Resources Dept.
- I.T. Department
- Audit expense
- Custodial Expenses
- Fringe Benefit and Operating Expenses associated with Indirect Cost Pool staff.





**IDC POOL**

**Finance**

**Purchasing**

**Audits**

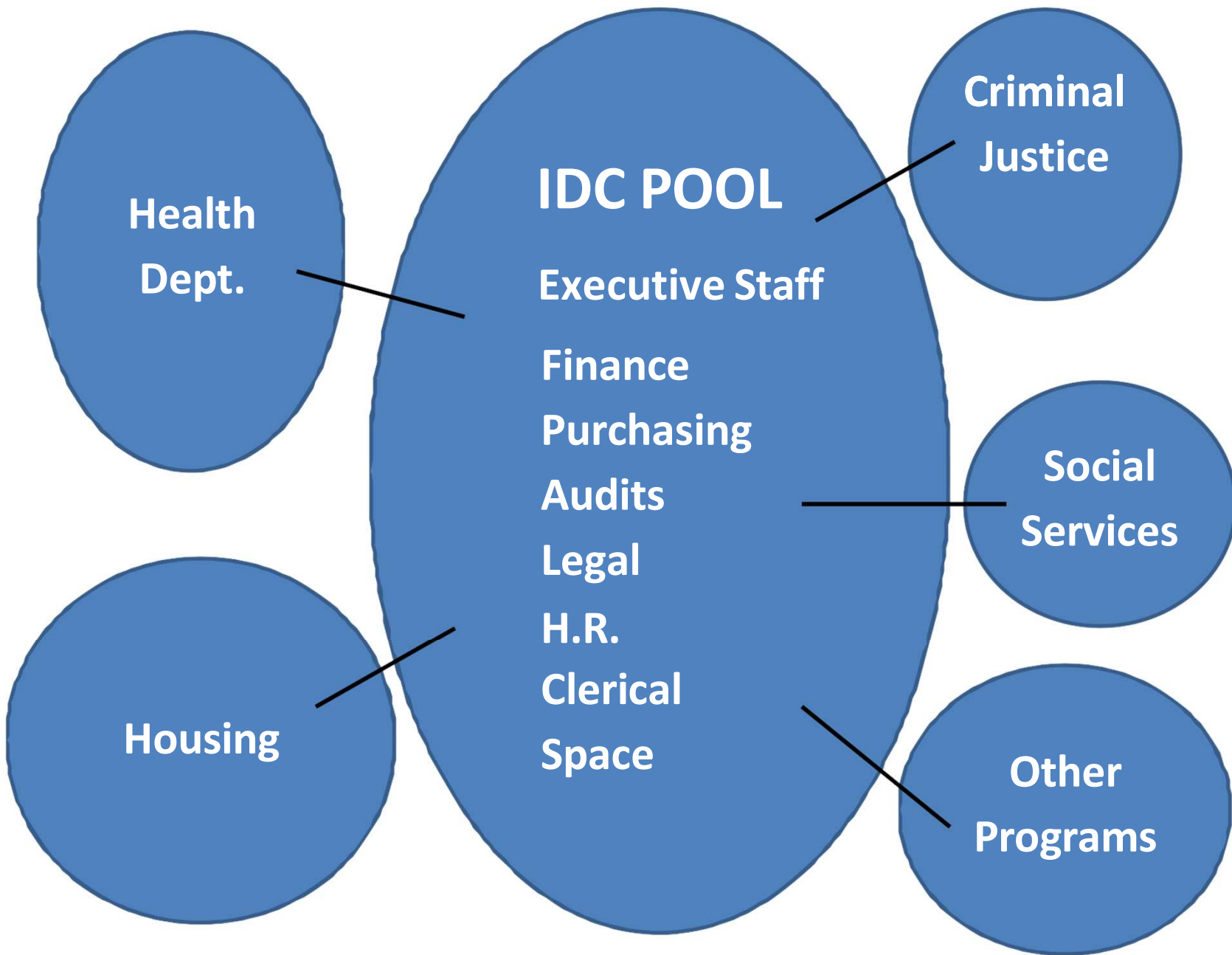
**Executive Staff**

**Legal**

**H.R.**

**Clerical**

**Space**

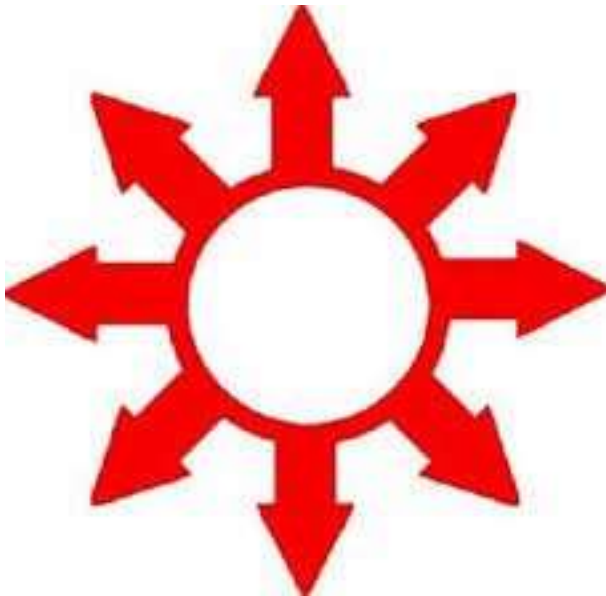




Program Revenue	71,280		86,583		130,739		
IDC Revenue							7,500
	<b><u>Program A</u></b>		<b><u>Program B</u></b>		<b><u>Program C</u></b>		
Salaries	25,000		30,000		45,000		24,500
Fringe	8,000		9,600		14,400		7,840
Rent	2,500		3,000		4,500		7,500
Travel	10,000		8,000		15,000		6,000
Contractual	5,000		8,000		12,000		15,000
Supplies	2,500		5,000		5,000		5,500
All other direct costs	1,000		1,500		2,400		2,000
<b>Total Direct charges</b>	<b>54,000</b>		<b>65,100</b>		<b>98,300</b>		<b>68,340</b>
<i>/DC Charge to program 33%</i>	17,820		21,483		32,439		
<b><u>Total Charges to Program</u></b>	<b><u>71,820</u></b>		<b><u>86,583</u></b>		<b><u>130,739</u></b>		<b><u>68,340</u></b>

# Which is a Better Representation of the Way the Cost Allocation Process Works?

A.



B.



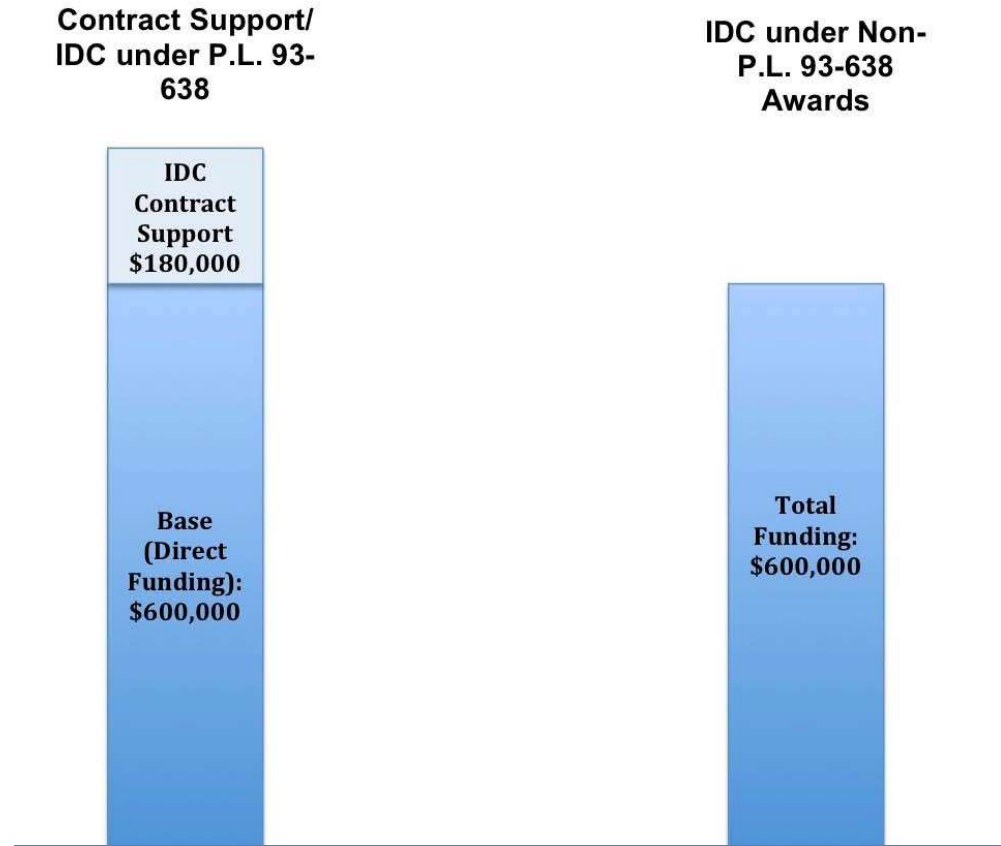
C. Both

## P.L. 93-638 Funding vs. Non-P.L. 93-638 Funding

Example:

Your Tribe gets a \$600,000 contract.

Your Indirect Cost Rate is 30%.



The IDC of \$180,000 is added to the program base

(Total funding becomes \$780,000)

IDC comes out of the Total Funding.

(The program will use \$180,000 of the \$600,000 funding for IDC, leaving \$420,000 to spend on Direct Costs)

## Calculating Direct on Non 638 grants and contracts

How do I determine how much Direct dollars I have to spend before I begin budgeting?

### Example of \$500,000 Total Funding

Assuming an IDC rate of 33%

$$Y \times 1.30 = 500,000$$

$$Y = 500,000 / 1.33$$

$$Y = \$375,940$$

In this example the program would have \$375,940 to budget toward direct expenditures assuming no pass throughs or other capital expenditures.

Direct = \$375,940

Indirect = \$124,060

Total= \$500,000



# The Base



**A.K.A. Distribution (Allocation) Base;  
Direct Cost Base**

"Base" means the accumulated *direct* costs (normally either total direct salaries and wages or total direct costs exclusive of any extraordinary or distorting expenditures) used to distribute indirect costs to individual Federal awards.

- The base is the denominator of the IDC Rate

# The Base

The direct cost base selected should result in each award bearing a fair share of the indirect costs in reasonable relation to the benefits received from the costs.



# Commonly used distribution bases include the following:

- Direct salaries and wages including applicable fringe benefits
- Direct salaries and wages excluding fringe benefits
- Modified total direct costs (MTDC) (more on this later)







# Excluded Costs

- Certain types of costs (activities) require relatively minimal administrative support compared to the amount of dollars spent. These costs would distort the indirect cost process and are excluded from the calculation of the indirect cost rate.
- Other costs are specifically excluded by regulation.

# Excluded Costs Include:

- Capital outlay
  - ex: expenditures for items such as the acquisition of land, improvements to sites, construction or purchase of new buildings, capitalized equipment)
- Pass-throughs or flow-throughs
- Debt service



# Excluded Costs Include:

- Judgments or Leans
- Certain transfers

Indirect cost recoveries are also categorized as excluded costs.

**EXCLUDED**

# Flow-Through Funds (or Pass-Through Funds)

Funds that are distributed to a primary recipient and subsequently passed through to another organization that actually performs the program for which the funds are provided.

- No measurable involvement by the primary recipient in the expenditure of the funds.
  - Just monitoring and oversight.



# Flow-Through Funds (or Pass-Through Funds)

Pass Through/Flow through costs are excluded from the indirect cost rate's base. Examples:

- Large subcontracts
- Recipient stipends
- Scholarships
- And capital expenditures



Why do you think these funds would be excluded from the base?

# Over-Recovery

When you collect more indirect costs than you have spent over a given period

What are consequences of over-recovery?



# Under-Recovery

When you collect fewer indirect costs than you have spent over a given period

What are consequences of under-recovery?





# What are Your Questions about Flow-Through, Exclusions, or Over-recovery?



# Indirect Costs Jeopardy



# Indirect Costs for \$100

This makes up the denominator of the formula for the Indirect Cost Rate.

# Indirect Costs for \$200

This makes up the numerator of the formula for the Indirect Cost Rate.

# Indirect Costs for \$500

This is all the Tribe's accumulated costs that jointly benefit 2 or more programs (**indirect costs**).

# Indirect Costs for \$600

This is made up of the Tribe's accumulated **direct** costs.

# Indirect Costs for \$700

These are costs that are left out of the calculation of the Indirect Cost Rate because they would distort the indirect cost process, or because regulation prohibits them.

# Indirect Costs for \$800

This is when you collect more indirect costs than you have spent over a given period.



# Indirect Costs for \$900

This is when you collect fewer indirect costs than you have spent over a given period.

# Module 5: Indirect Cost Rates



4 Friends Go Out to Dinner. 3 get a steak, and one gets a salad.

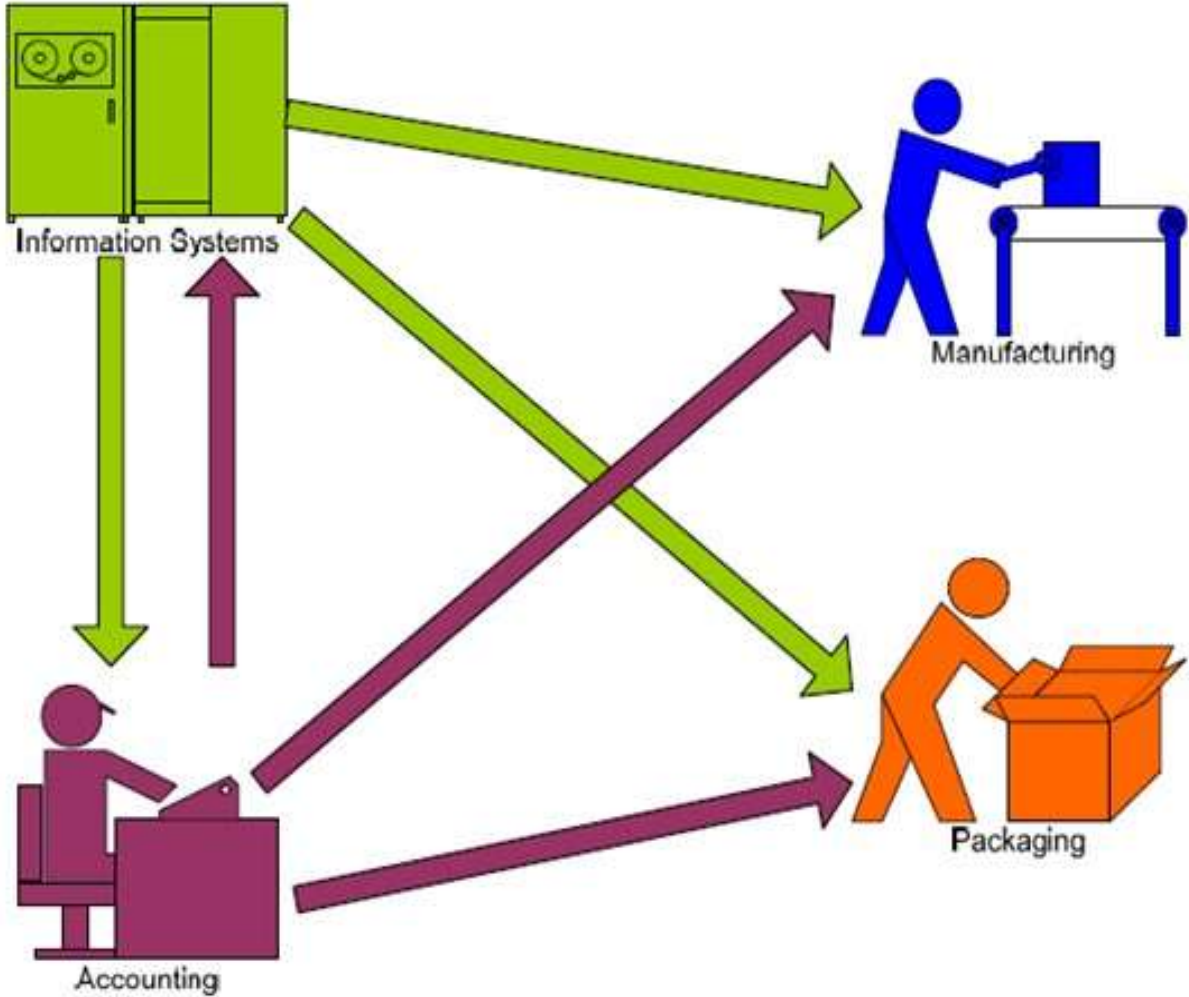
What are Different Ways They Could Split The Bill?



# How Does Your Tribe Decide How it Will Fairly Allocate Costs?

Support Departments

Production Departments



# Indirect Cost Rate

- Indirect costs are normally charged to Federal awards by the use of an **indirect cost rate**.

The IDC rate is a mechanism for determining, fairly and conveniently, what proportions of Departmental/organization *administration* costs each individual program should bear.



# Indirect Cost Rates are Used Both For:

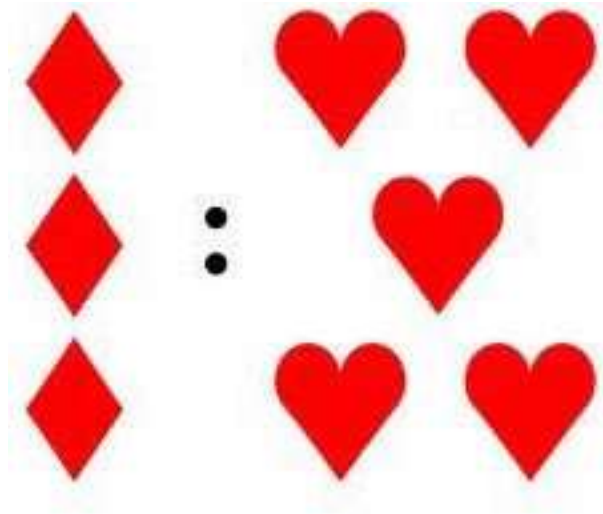
- Funding indirect costs



- Charging indirect costs

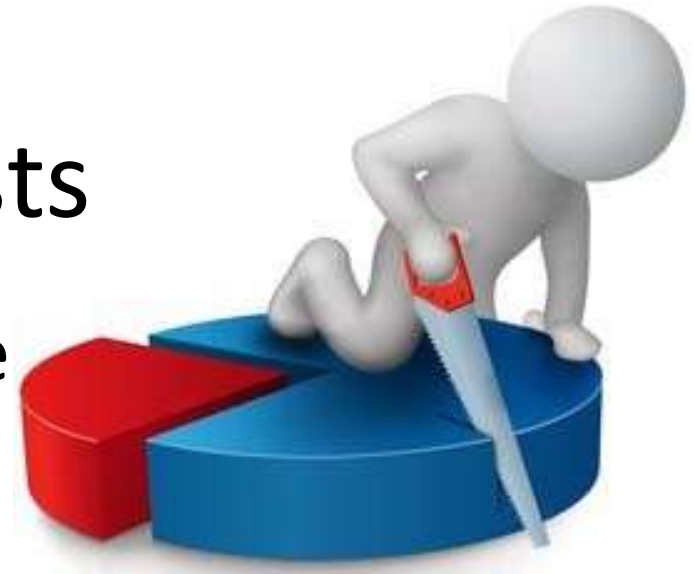
**INVOICE**

In general terms, an indirect cost rate is the percentage of an organization's indirect costs to its direct costs.



# Unallowable Costs

Costs that are not allowed to be charged to a federal project



- Unallowable costs are excluded from the Indirect Cost Rate and from Indirect Cost Pools
  - So, when we budget for indirect costs, we exclude these costs



# Unallowable Costs



- Specifically identified in the grant/contract as being unallowable
- Specifically identified in Circular A-87 (or the Super Circular for awards made after Dec 26, 2014) as being unallowable
- Does not meet the criteria listed in Circular A-87 (or Super Circular) to be allowable

# Why an IDC Rate is Necessary

Used for:

- Management information
  - Why/when do YOU think it would be useful here?
- To be in compliance with Federal regulations, (e.g. A-87/Super Circular)
- Close-out purposes
- Audit documentation



# Why an IDC Rate is Necessary

Unless you have a very small organization, determining indirect costs by calculating actual usage on a case-by-case basis would be very hard to keep track of.

Having an IDC rate simplifies it.



**simple is  
beautiful.**

The indirect cost rate can be used to budget the amount of indirect costs allowable for a program (so you won't go over budget) and then to claim the actual amount of indirect costs after the program expenditures have been made.

*It is important to remember that when recovering/charging indirect costs, the indirect cost rate is applied to the amount actually expended, not the total amount budgeted.*