March 4: Does Our CAA Effectively Estimate and Reconcile Indirect Costs?

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Negotiated Indirect Cost Rate Choices - REVISED

CAPLAW Indirect Cost Series –Part 3
February 25, 2015
Workshop Leader: Kay Sohl

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OMB’s Uniform Guidance
2 CFR 200

• Published at Code of Federal Regulations on December 26, 2013
• Implementation Regulations published on December 19, 2014
• Effective for awards that begin after 12/26/14 & audits of fiscal years beginning after 12/26/14

Big Change for Indirect Costs

• All federal agencies & pass-through entities must accept approved NICR - negotiated indirect cost rate

• Pass thru entities are required to either allow sub-recipients to negotiate indirect rate or use a flat indirect rate of 10% of MTDC (modified total direct costs)
Big Change for Indirect Costs

• Uniform Guidance permits extension of NICR timeframe
• Alternative to negotiating every year
• May request extension of approved rate for up to 4 years
• If extension granted, may not negotiate again until end of extension period

Exceptions to Uniform Guidance

• Federal statutes override Uniform Guidance
• Federal agencies may have statutory authority to limit or disallow certain costs
Uniform Guidance: 3 Ways to Recover Indirect Costs

• Negotiated Indirect Cost Rate- NICR

• 10% de minimis rate

• Direct charging through cost allocation

Negotiated Indirect Cost Rate

• Recipients & sub-recipients negotiate rates with their federal cognizant agency
• Cognizant agency is usually the entity’s largest source of federal $
• Sub-recipients without direct federal awards generally cannot negotiate indirect cost rates with federal agencies
Potential Catch 22

• 10% de minimis rate is available to recipients and sub-recipients that have never had a NICR

• NICR must be current in order to be protected by “must allow” provisions of Uniform Guidance

• ?? Entites with prior NICR but no current NICR and no direct federal award ??

NICR Negotiation Process

• Identify cognizant agency

• Clarify negotiating process

• Submit proposed NICR – using estimated costs

• Review and revise if required

• Receive NICRA – Negotiated Indirect Cost Rate Agreement
NICRA Establishes Timeframe for Use of Rate

- **Provisional rate**: temporary, based on estimated costs-subject to adjustment
- **Final rate**: based on actual costs
- **Predetermined rate**: not subject to adjustment
- **Fixed rate with carry forward**: adjustment made in future periods

Provisional Rates Most Common for Newer or Smaller Entities

- Rate proposal uses estimated costs for fiscal year
- Requires submission of audited financial info within 6 months of the end of fiscal year
- True-up process used to determine if provisional rate was under or over actual rate
Indirect Cost Rate: Based on a Fraction

Numerator = Indirect Costs

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Denominator = Direct Costs

• Must make choices about both

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Defining Indirect Costs

• Must include administrative costs which benefit entire entity

• May include other common or shared costs which benefit entire entity:
  • Facilities
  • Telephone/internet
  • Copiers, etc.

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Administrative Costs Include

- Accounting & fiscal management
- Board support
- HR management
- IT management
- Agency-wide strategic planning
-Executive management

Not All Admin Costs are Indirect

- Administrative functions that benefit only one or a limited number of programs/awards may be treated as Direct Costs

- Example:
  - Accountant performing only Head Start functions
Numerator Choices for NICR

• **Direct Allocation Method**
  Indirect = Admin costs only

• **Simplified Allocation Method**
  Indirect = Admin plus facilities & other shared costs

More Numerator Choices

• **Multiple Rate** – involves use of multiple Indirect Cost Pools

• **Special Rate** - used to address distorting factors – typically negotiated with larger entities
Only Allowable Indirect Costs in Numerator

- All methods of computing the Indirect Cost numerator require excluding unallowable indirect costs
- Example:
  - Alcohol served at Board functions

3 Choices for the Direct Cost Base (Denominator)

- Direct Salaries & Wages (including compensated absences)
- Total Direct Salaries & Wages (including employer PR tax & fringe benefits)
- Modified Total Direct Cost: MTDC
All Bases Must Include All Direct Costs

- **Direct cost base:** must include direct costs funded through private sources as well as fed sources
- Must include direct costs that are unallowable for federal funds
- Use of Modified Total Direct Costs as base requires exclusion of some direct costs

## NICR using MTDC Base

<table>
<thead>
<tr>
<th>TOTAL Expenses</th>
<th>Unallow indirect costs</th>
<th>Excluded direct costs</th>
<th>Indirect costs</th>
<th>MTDC</th>
<th>award 1 direct</th>
<th>award 2 direct</th>
<th>award 3 direct</th>
<th>non-fed direct cost</th>
</tr>
</thead>
<tbody>
<tr>
<td>4,450,000</td>
<td>10,000</td>
<td>40,000</td>
<td>800,000</td>
<td>3,600,000</td>
<td>1,000,000</td>
<td>1,740,000</td>
<td>660,000</td>
<td>200,000</td>
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</tbody>
</table>

| Allowable indirect | 800,000 |
| MDTC              | 3,600,000 |
| Indirect rate      | 0.222   |
### Applying the MTDC Indirect Rate

<table>
<thead>
<tr>
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<td>1,740,000</td>
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<td>200,000</td>
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</tbody>
</table>

| Indirect Rate  | 222                    | -800,000              | 800,000        | 222,222      | 386,667       | 146,667       | 44,444         |
| Excluded costs | -40000                 |                       | 40,000         |              |               |               |                |
| Unallow indirect costs | -10000               |                       |               |              |               |               |               |
| Total Costs    | 0                      | 0                     | 0              | 1,222,222    | 2,126,667     | 846,667       | 254,444        |

### NICR using Total Direct Salaries Base

<table>
<thead>
<tr>
<th>TOTAL Expenses</th>
<th>Total Costs</th>
<th>Unallow indirect costs</th>
<th>Indirect costs</th>
<th>Direct Costs</th>
<th>award 1 direct</th>
<th>award 2 direct</th>
<th>award 3 direct</th>
<th>non-fed direct cost</th>
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</thead>
<tbody>
<tr>
<td>Salaries &amp; Fringe Benefits</td>
<td>3,600,000</td>
<td>600,000</td>
<td>3,000,000</td>
<td>800,000</td>
<td>1,500,000</td>
<td>520,000</td>
<td>180,000</td>
<td></td>
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<tr>
<td>Other Expenses</td>
<td>850,000</td>
<td>10,000</td>
<td>200,000</td>
<td>640,000</td>
<td>200,000</td>
<td>180,000</td>
<td>20,000</td>
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</tr>
<tr>
<td>Total</td>
<td>4,450,000</td>
<td>10,000</td>
<td>800,000</td>
<td>3,640,000</td>
<td>1,000,000</td>
<td>1,740,000</td>
<td>700,000</td>
<td>200,000</td>
</tr>
</tbody>
</table>

| Allowable Indirect | 800,000 |
| Total Direct Salaries & Fringe Benefits | 3,000,000 |

Indirect rate: 0.267
### Applying Total Direct Salaries Base Rate

<table>
<thead>
<tr>
<th></th>
<th>Unallow indirect</th>
<th>Allowable indirect</th>
<th>Total Costs</th>
<th>award 1</th>
<th>award 2</th>
<th>award 3</th>
<th>non-fed</th>
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<tr>
<td><strong>TotalDirect Salaries</strong></td>
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<td>Allowable Indirect Costs</td>
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<td>800,000</td>
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<tr>
<td>Indirect Rate 27%</td>
<td>-800,000</td>
<td>800,000</td>
<td>213,333</td>
<td>400,000</td>
<td>138,667</td>
<td>48,000</td>
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<tr>
<td>Other Direct Exp</td>
<td>10,000</td>
<td>640,000</td>
<td>200,000</td>
<td>240,000</td>
<td>180,000</td>
<td>20,000</td>
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<tr>
<td>Unallow indirect alloc</td>
<td>-10,000</td>
<td>10,000</td>
<td></td>
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<td></td>
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<tr>
<td><strong>Total Costs</strong></td>
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<td>0</td>
<td>1,450,000</td>
<td>1,213,333</td>
<td>2,140,000</td>
<td>838,667</td>
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### NICR using Direct Salaries Base

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<tr>
<td><strong>Salaries Only</strong></td>
<td>2,640,000</td>
<td>440,000</td>
<td>2,200,000</td>
<td>588,000</td>
<td>1,100,000</td>
<td>800,000</td>
<td>132,000</td>
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<tr>
<td><strong>Other Expenses</strong></td>
<td>1,810,000</td>
<td>10,000</td>
<td>360,000</td>
<td>1,440,000</td>
<td>412,000</td>
<td>640,000</td>
<td>320,000</td>
<td>68,000</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>4,450,000</td>
<td>10,000</td>
<td>800,000</td>
<td>1,640,000</td>
<td>1,000,000</td>
<td>1,740,000</td>
<td>700,000</td>
<td>200,000</td>
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| Allowable Indirect Costs | 800,000 |
| Direct Salaries Only | 2,200,000 |

| Indirect rate | 0.364 |
Applying Direct Salaries Base Rate

<table>
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<tr>
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<td>800,000</td>
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<td>47,500</td>
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<tr>
<td>Indirect Rate 36%</td>
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<td>10,000</td>
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<tr>
<td>Total Costs</td>
<td>0</td>
<td>4,450,000</td>
<td>1,213,500</td>
<td>2,140,000</td>
<td>839,000</td>
<td>257,500</td>
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3 Bases Result in 3 Different Indirect Rates

- MTDC Example: 22.2
- Total Direct Salaries Base: 26.7%
- Direct Salaries Base: 36.4%
All 3 Bases Result in the Same Total Recovery of Indirect Costs

- Choice of base may impact the indirect cost burden charged to your distinct programs or awards
- Choice of base & resulting NICR may create more or less resistance from private funders

Which Base Will Yield Highest Indirect Cost Rate?

- Direct Salaries and Wages provides smallest denominator and yields highest indirect %
- Total Direct Salaries & Wages (including employer taxes & benefits) yields next highest indirect %
- MTDC yields lowest indirect %
Impact of Numerator on Rate

- Direct Allocation Method includes only indirect Admin Costs in Indirect
- Simplified Allocation Method includes indirect Admin Costs & Facilities & Common Costs
- Direct Method results in smaller numerator = lower rate

Indirect Cost Proposal Steps

- Develop master schedule of all cost centers – direct and indirect
- Identify the costs to be included in the indirect cost center
- Identify direct cost center structure:
  - Each award = a cost center
  - Each program = a cost center (which may be supported by multiple awards)
Proposal Must Include All Costs for Agency Fiscal Year

- **Indirect costs**
  - Allowable for federal $$
  - Unallowable
- **Direct costs**
  - Allowable for federal $$
  - Unallowable
  - Includes costs met through non-federal sources

Choices

- Negotiate a NICR?
- Request extension for your NICR?
- Simplified or Direct Allocation method?
- Which Base?
- Seek predetermined or fixed rate?
Follow-up Webinar

• March 4, 2015
• Estimating and Reconciling Indirect Costs
  o Impact of over and under estimating indirect cost rates
  o Dealing with statutory limitations on admin and indirect costs