A GUIDE FOR NONPROFIT ORGANIZATIONS

Cost Principles and Procedures for Establishing Indirect Cost Rates with the U.S. International Agency For International Development

July 1995

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PREFACE

This guide has been developed to help nonprofit organization: t have assistance instruments and contracts with the United States Agency for International D opment (USAID) understand the process for determining and reimbursing indirect costs unc JSAID awards/contracts.

The Office of Management and Budget (OMB) Circular A-12 Cost Principles for Nonprofit Organizations" provides the cost principles that govern direc d indirect cost applicable to nonprofit organizations. This circular defines indirect cost as e that have been incurred for common or joint objectives and cannot be readily identified wit particular final cost objective. It also defines a nonprofit organization as any corporation, t association, cooperative, or other organization which (1) is operated primarily for scientifi ucational, service, charitable or similar purposes in the public interest; (2) is not organized narily for profit; and (3) uses its net proceeds to maintain, improve, and/or expand its oper. s.

Provided within this guide are illustrative examples of vari indirect cost rate structures which should not be viewed as required formats by U). The indirect cost rate structure chosen by an organization depends on spec factors applicable to the organization.

This guide was developed by Steven Tashjian and James Deery of the e of Procurement, Procurement Support Division, Office of Overhead/Special Costs and Contra oseout Branch of USAID.

Definitions

For purposes of this guide, the following definitions are provided:

Administrative Expenses

All direct and indirect costs associated with the management of an organization's programs. Nonprofit organizations need to refer to their grant/cooperative agreement/contract terms and conditions for the applicable definition of "Administrative Costs" and any related limitations.

Allocation Base

The costs which are used as the denominator in the indirect cost rate calculation. These cost represent an organization's choice as to what activity has the best causal beneficial relationship with the indirect cost pool. The base chosen should result in an equitable distribution of indirect cost.

Cost Objective

A function, organizational subdivision, award, contract, or other work unit for which cost data are desired and for which provision is made to accumulate and measure the cost of processes, products, jobs, capitalized projects, etc.

Direct Costs

Those costs that can be specifically identified with a particular final cost objective, i.e., a particular award, project, service,or other direct activity of an organization.

Final Cost Objective

A cost objective that has an allocation of both direct and indirect costs and, in the organization's accumulation system, is one of the final accumulation points.

Final Rate

An indirect cost rate applicable to an accounting period (fiscal year) which is based on the audited actual costs of the period. A final rate is not subject to adjustment.

Indirect Cost

Those cost that have been incurred for common or joint objectives and cannot be readily identified with a particular final cost objective.

Indirect Cost Pools

Groupings of costs identified with two or more cost objectives but not specifically identified with any final cost objective.

Indirect Cost Proposal

An organization's supporting documentation for the establishment of an indirect cost rate(s), so it can be reimbursed it's indirect cost.

Indirect Cost Rate

The ratio of total indirect cost to its allocations base, expressed as a percentage. The indirect rate serves as the vehicle for reimbursement/funding of indirect cost.

Nonprofit Organization

Any corporation, trust, association, cooperative, or other organization which (1) is operated primarily for scientific, educational, service, charitable or similar purposes in the public interest; (2) is not organized primarily for profit; and (3) uses its net proceeds to maintain, improve, and/or expand its operations.

Provisional Rate

A temporary indirect cost rate applicable to a specified period which is used for funding, interim reimbursement, and reporting indirect costs on awards pending the establishment of a final rate for the period.

SECTION II

A. Indirect Cost Rates

An organization's cost that are identified with two or more cost objectives but do not directly benefit any one final cost objective are termed indirect cost. These cost are budgeted, billed and accounted for via an indirect cost rate or rates. This rate is developed by determining what direct cost have a casual beneficial relationship with the indirect cost. This relationship furnishes the basis for developing an indirect rate. The cost which are determined to drive the indirect cost represent the allocation base. The base selected must result in an equitable distribution of indirect cost. The indirect cost rate is derived by determining the ratio of indirect cost to the allocation base cost. There are many different specific indirect cost rate methodologies available to determine an organization's indirect cost rate(s). These specific indirect cost rate structures are explained further in Part B of this section.

A variety of indirect cost rate types are available, which are described as follows:

<u>Provisional Rate</u>

A provisional rate is a temporary rate for an established period of time to facilitate budgeting and billing of indirect cost until a final rate can be established. These provisional rates are adjusted after the incurred cost for the period are known and a final rate has been established.

<u>Final Rate</u>

A final indirect cost rate is established after the cost incurred for an established period are known and the amount of allowable cost applicable to Federal awards is determined. A final rate is not subject to adjustment once established. Final rates are used to adjust rates which were awarded on a provisional basis. Often, a final rate is used as the basis for establishing a provisional rate for the next accounting period, after it has been adjusted for known differences in cost levels.

<u>Predetermined Rate</u>

A permanent indirect cost rate is a rate assigned for a specific period of time which is not subject to adjustment. A predetermined rate is used only when there is substantial assurance that the predetermined rate will not exceed the actual rate incurred for the applicable period.

Fixed Rate with Carry-Forward Provision

A fixed rate with a carry-forward provision is similar to a predetermined rate, except that the difference between the estimated cost used to establish the fixed predetermined rate and the actual cost for the period is "carried forward" as an adjustment to the rate computation for a future year(s).

Selection of Rate Type

USAID prefers the use of the provisional/final rate indirect costing system for nonprofit organizations for a variety of reasons. Primarily, it necessitates an accounting system which can generate current accurate cost data. This ability helps both the nonprofit organization and USAID make informed budgeting and funding decisions. Second, indirect cost are properly funded in the fiscal year incurred. Thus, there are no prior year "carry forward" adjustments to be made in future years due to a difference between a negotiated predetermined rate and the actual rate incurred for the period, which can effect current and out-year funding. Finally, it allows for an adjustment of indirect cost at year end to account for the difference between the provisional rate and the actual rate incurred so a significant cost discrepancy does not exist when the award is being closed out.

B. Determination of Indirect Cost Rate Structure

The Governing principles for nonprofit organizations regarding indirect costs are prescribed in the OMB Circular A-122, "Cost Principles for Nonprofit Organizations." This circular provides specific methods for distributing indirect cost to final cost objectives. These methods and the criteria to determine which is appropriate are explained below.

Simplified Allocation Method

When an organization's functions all benefit from indirect cost in the same degree or there is only one major function, a simplified allocation method generally results in an equitable distribution of indirect cost. In this scenario an organization would arrive at its indirect cost rate by separating the total cost for the period into direct and indirect cost and dividing the total allowable indirect costs by an equitable distribution base. Thus, this rate, expressed as a percentage, represents the relationship of the indirect cost to the chosen allocation base.

Care must be taken when choosing the allocation base to ensure it accurately represents the best relationship between indirect cost and the base available. Two examples of allocation bases are total direct cost (excluding capital expenditure and other distorting items, such as major subcontracts or subgrants) and direct labor cost.

Except where a special rate is required as explained below, the rate(s) developed must be applied to all awards of the organization.

An example of the process involved when developing indirect rates under the Simplified Allocation Method is provided in Section IV of this guide.

For more specifics regarding this rate methodology, see the OMB Circular A-122, Section D.2.

Multiple Allocation Base Method

When an organization has more than one major function and these functions do not all benefit from indirect cost in the same degree, the multiple allocation base method should be utilized. Under this method, the indirect cost need to be accumulated into homogenous cost groups, which will be allocated to the benefiting functions by means of a base which best measures the relative benefits. The number of separate groupings should be minimized and based on the materiality of the cost involved and the degree of accuracy required. An indirect cost rate will need to be developed for each individual cost grouping. The indirect costs are then allocated to each award and other direct activities included in the allocation base via the indirect cost rate(s).

In accordance with the OMB Circular A-122, Section D.1.c., "the determination of what constitutes an organization's major functions will depend on its purpose in being; the types of services it renders to the public, its clients, and its member; and the amount of effort it devotes to such activities as fund raising, public information and membership activities."

The criteria required to justify the use of the multiple allocation base method rarely exists within USAID awarding/contracting environment. Accordingly, we have not included an example of the process involved when developing indirect rates under the Multiple Allocation Base Method However, an example of this method is available in the Department of Health and Human Services publication, OASMB-5, entitled "A Guide for Nonprofit Organizations."

For more specifics regarding this rate methodology, see the OMB Circular A-122, Section D.3.

Direct Allocation Method

The direct allocation method is appropriate when an organization wishes to treat all cost as direct except for general administration and general expenses. These organizations generally separate their costs into three basic categories; (i) general administration and general expense, (ii) fund raising, and (iii) other direct functions. Joint costs, such as depreciation, rental costs, operation and maintenance of facilities, telephone expense, and the like are prorated individually as direct costs to each category and to each award or other activity using a base most appropriate to the particular cost being prorated. Each joint cost is then distributed based on an equitable allocation base. The bases chosen must accurately measure the benefits provided to each award or activity and be based on reasonable criteria and current data. Examples of allocation bases for common joint cost are listed in Exhibit E of Section IV. The allocation method for the single indirect cost rate is the same as the simplified allocation method, except that the indirect cost consist exclusively of general administration and general expenses.

An example of the process involved when developing indirect rates under the Direct Allocation Method is provided in Section IV of this guide.

For more specifics regarding this rate methodology, see the OMB Circular A-122, Section D.4.

Special Indirect Cost Rates

Generally, the use of the other three allocation methods described above result in an equitable distribution of indirect cost to final cost objectives. However, in some instances, a single indirect cost rate for all activities or for each major function of an organization may not be appropriate, as it does not take into account distorting factors which may substantially affect the allocation of indirect cost. This scenario generally occurs when an activity performed by the organization is materially different then its normal line of business and thus generates a significantly different amount of indirect cost. In these cases, provisions should be made to have the cost accumulated in a separate indirect cost pool and allocated on a more equitable basis. The use of this rate methodology is only warranted when it is determined that the rate differs significantly from that which would have been obtained under the other methods available and the volume of work to which the rate would apply is material.

An example of the process involved when developing indirect rates under the Special Indirect Cost Rates method, is provided in Section IV of this guide.

For more specifics regarding the use of the special indirect rate methodology, see the OMB Circular A-122, Section D.5.

Selection of Rate Methodology

The choice of the appropriate rate methodology for an organization requires careful consideration and review of such factors as the: (i) sophistication of the accounting system in place, (ii) degree of precision desired/needed, (iii) amount of funding involved (materiality), (iv) cost of degree of accuracy desired verse benefits received, (v) number of awards involved, (vi) number of employees, and (vii) availability of data required (hours of machine use, square footage, transactions processed, etc.). These factors need to be evaluated with the intent of employing a rate methodology that equitably distributes indirect cost to final cost objectives. The goal should be to use a rate methodology which results in an equitable distribution of indirect cost (i.e., no material inequities exist) without being overly cumbersome or costly. As a organization becomes more sophisticated by expanding into new areas of business, so should the level of accounting data required.

General Information

For purposes of calculating the allowable indirect cost rate(s) for U.S. awards, all unallowab cost must be excluded from the total indirect cost pool before dividing by the allocation base to arrive at the resulting indirect rate. Unallowable cost are identified in Section B of the OMB Circular A-122. Examples of unallowable cost are bad debt expense, entertainment cost, interest expense, and losses on Federal or non-Federal awards. However, all cost which normally would be in the allocation base remain in the allocation base whether deemed allowable or unallowable by the criteria in the OMB Circular A-122, so that they bear their pro rata share of indirect cost.

The base period used for the development of the indirect cost rate should be the same as the organization's fiscal year.

C. Changing an Indirect Rate Structure

Prior approval from the Office of Procurement, Procurement Support Division, Office of Overhead/Special Costs and Contract Closeout Branch (OCC) of USAID must be obtained before an organization can change the way it allocates cost. Once an organization has awards and contracts with USAID, based on an accepted established indirect cost rate structure, agreement has been reached on how cost are to be allocated to awards/contracts. Accordingly, any modification of the allocation methodology constitutes a change in these agreements and thus requires prior approval from USAID. Failure to obtain approval may result in cost disallowances.

When an organization has determined that it wishes to change the way it allocates indirect cost, it needs to prepare a proposal supporting such a change and submit it to the OCC Branch. Such a proposal would need to include the following:

1. A narrative explanation of the proposed change and why it is warranted;

2. A cost impact analysis showing the impact of the new rate structure on each award. This analysis should use actual data from the most completed fiscal year and compare the cost for each award under the old and proposed rate structure. The major cost elements (i.e., direct labor, ODCs, subawards, materials, and each indirect cost grouping) should be shown for each award, and

3. An accurate description of how the composition of the indirect cost pool and base cost changed from the old rate structure to the proposed new rate structure, both in narrative form and cost schedule form.

Upon receipt of such a proposal the cognizant Contract Specialist within OCC will evaluate the proposal and coordinate directly with an organization's representative. Once a mutual agreement has been reached regarding the proposed change, a revised NICRA will be issued reflecting the accepted rate structure.

It is important to remember that approval is required before the change has taken place. Failure to obtain prior approval can result in a disallowance of cost.

D. Approval Process

Every organization intending to establish indirect cost rates applicable to Government awards and contracts must develop an indirect cost proposal. This indirect cost proposal forms the basis for all negotiations regarding the applicable indirect cost rate(s). Guidelines for preparing an adequate indirect cost proposal are contained in Sections III & IV and Appendix B of this guide.

Establishing an Initial Provisional Indirect Cost Rate(s) When no Previous Rate(s) Existed

An indirect cost proposal should be submitted once an organization has been notified of an award that will allow for the reimbursement of indirect cost via an indirect cost rate. Generally, this proposal should be submitted as soon as possible after award. This proposal should be based on actual cost data adjusted for any known or expected deviations from historical experience. Normally a provisional indirect cost rate will be established based on the indirect cost proposal. Once an organization has established an adequate indirect cost rate structure approved by USAID, its provisional rates are generally updated on a yearly basis. They can be updated sooner when circumstances warrant it.

Modifying Provisional Indirect Cost Rates

At the completion of each fiscal year an organization should update it's provisional rate(s). Typically, provisional indirect cost rates are based on the previous year's actual rate experience. However, often an organization is aware of significant deviations from historical experience, such as the awarding or closing of a grant. Such deviations should be incorporated into the indirect cost proposal to improve the accuracy of forecasted rates.

If at any time an organization feels it's current provisional indirect cost rate(s) is materially misstated, (i.e. not reflective of actual cost to be incurred for the period) it should provide a revised indirect cost proposal to USAID so a more accurate provisional rate can be established.

Finalizing Indirect Cost Rates

Most nonprofit entities are governed b : OMB Circular A-133, "Audits of Institutions of Higher Learning and Other Non-Profit] ations." This circular currently requires a nonprof organization to submit an audit perform accordance with the circular within thirteen month of its fiscal year end. (This time fra expected to be reduced to nine months with the issuance of the revised OMB Circular .) Although not technically required, it is best for an organization to include a Schedule o rect Cost as part of the A-133 audit. This schedule and its supporting data will allow USAI finalize the organization's indirect cost rate(s). The cost principles in OMB Circular A-122 ost Principles for Nonprofit Organizations" govern the reasonableness, allowability and all ity of specific cost elements for nonprofit entities.

Audit Procedure

Once completed the A-133 audit is itted by the organization to the Contract Audit Management (CAM) Branch of USAI The CAM Branch will ask the USAID Office of Inspector General (IG) if it wishes to p m a Quality Control Review (QCR) of the subject audit. If the IG does not wish to perfo QCR, then the CAM Branch will perform a desk review. This desk review will determ hat audit recommendations require resolution and ensure the audit was performed in ac nce with professional and government standards. Once completed, the CAM Branch wil ward the report along with its recommendations to the Overhead/Special Costs and Contra oseout (OCC) Branch who will finalize the rates. If the IG determines it wishes to perfor QCR, it will forward the A-133 audit and the QCR to the CAM Branch upon completion of QCR. A copy will be furnished to OCC. However, under both scenarios, it is possible t e audits provided the OCC Branch will include recommendations covering various iss requiring resolution from many branches withi USAID. Final indirect cost rates can e determined until all recommendations effecting indirect cost rates have been resolved.

Approval of Indirect Cost Rates with grantees and Subcontractors

Prime grantees and contractors are resp e for approving indirect cost rates with subgrantees and subcontractors under the prime's ral award/contract. However, the Federal cost principles that apply to the prime, flow n to the subrecipients/subcontractors. The prime organization is not required to approve indirect cost rates when the subaward/subcontract does not allow reimbursement of indire t.

E. Negotiated Indirect Cost R Agreement (NICRA)

Formal approval of provisiona final indirect cost rates will be provided in a Negotiated Indirect Cost Rate Agreem NICRA). This NICRA is signed by the Chief of OCC and is to be signed by an autho representative of the organization. Pursuant to AIDAR 742.770, these indirect cost rate automatically incorporated into the awards shown in Part III of the NICRA.

Three copies of the NICRA will be provided to the organization. The organization should sign the original and the two copies of the NICRA, retaining one copy and returning the original and other copy as soon as possible to the OCC Branch Chief.

By execution, the signatory to this NICRA, acting on behalf of the organization, assumes full responsibility in assuring USAID that: (1) to the best of his/her knowledge the accounting information provided is complete and free from all inaccuracies; (2) the indirect costs claimed have not been and will not be claimed as direct costs or vice versa; (3) that similar types of costs have been accorded consistent treatment; (4) the incurred costs are legal and allowable in accordance with the governing cost principles and other federal regulations; and (5) that the information provided by the grantee/contractor which was used as the basis for acceptance of the rate(s) agreed to herein is not subsequently found to be materially incomplete or inaccurate.

For contracts, grants, or cooperative agreements which incorporate these rates, the organization should take the necessary actions to adjust their invoices for the difference between the billed and the indirect cost rates reflected in the NICRA. However, these negotiated rates shall not change any monetary ceiling, obligation, or specific cost allowance or disallowance provided for in each award between the parties.

For the negotiation of new awards with USAID Washington and overseas Missions, we advise the organization to provide copies of the NICRA and use the indirect cost rates stated therein. For the negotiation of new awards with other U.S. Federal Government agencies, we encourage the organization to provide copies of the NICRA and use the indirect cost rates stated therein.

Any change in the accounting system which affects any component of the incurred cost requires prior approval from the OCC Branch. Failure to obtain such approval may result in cost disallowances.

Each NICRA will include the following:

1) Identification of the indirect rate as either final or provisional;

2) The effective period for each rate(s);

3) The rate(s) itself expressed as a percentage;

4) Description of the allocation base for each rate;

5) A listing of the Contracts/Grants/Cooperative Agreements effected by the NICRA and:

6) General terms and conditions.

An example of a NICRA is included in Appendix A of this guide.

F. Application of Indirect Cost Rates

The amount of reimbursable indirect cost allowable on Federal awards will be determine by multiplying the approved indirect cost rate(s) by the approved allocation base(s) of each award. The approved indirect cost rate(s) and allocation base(s) will be defined in the Negotiated Indirect Cost Rate Agreement (NICRA). However, in those instances where a Federal award has an indirect cost rate ceiling, indirect cost will only be reimbursed up to the amount of the limitation cited in the award. Also, whenever the performance of an award covers multiple fiscal years, the approved indirect cost rate(s) for each year(s) must be applied to the allocation base cost incurred.

For an illustration of these principles assume the following data:

Period	Approved Indirect Cost Rate
01-01-93 to 12-31-93	15%
01-01-94 to 12-31-94	10%

The approved allocation base is total direct cost and the grant period of performance is 03-01-93 to 12-31-94.

The total direct cost incurred for the program is $500,000, incurred by year as follows:
Incurred in 1993 $100,000
Incurred in 1994 $400,000

Determination of Indirect Cost
1993 cost of $100,000 x .15 = $15,000
1994 cost of $400,000 x .10 = 40.000
Total Indirect Cost $55.000

Now assume that the grant had a ceiling limitation on the indirect cost rate of 12 percent. Assuming all other data is the same, the applicable indirect costs would be determined as follows:

Determination of Indirect Cost
1993 cost of $100,000 x .12 = $12,000
1994 cost of $400,000 x .10 = 40.000
Total Indirect Cost $52.000

G. Limitations on Indirect Cost

Indirect cost limitations are negotiated into some Federal awards/contracts. In these instances, indirect cost will be reimbursed up to the amount of the limitations cited in the awards/contracts. If the amount of indirect cost incurred are above the ceiling limitations in a federal award/contract, the excess amount may not be shifted to other federal awards/contracts, unless specifically authorized by legislation.

H. Disputes

In the unlikely event that the Office of Overhead/Special Costs and Contract Closeout (OCC) Branch and the Grantee/Contractor are unable to reach a mutual agreement on an acceptable indirect cost rate(s), the OCC branch will issue a unilateral determination of the rate(s). The OCC branch will notify the organization of such a determination and advise what right of appeals apply and the appropriate procedures to follow. The effected grants/contracts will include a disputes clause which outlines the procedures to be followed.

SECTION III

A. Submission of Indirect Cost Proposal

An adequate indirect cost rate proposal forms the basis for all negotiations regarding the allowability and allocability of indirect cost for Federal awards. Accordingly it is very important that this proposal be prepared with care and in a timely fashion.

Required Documentation for an Adequate Indirect Cost Proposal

Following is a list of required information for an adequate indirect cost rate proposal:

1. Indirect cost pool schedules detailing the cost by cost element for each indirect cost rate, including identification of unallowable cost,

2. Schedule of labor cost for all employees, identifying annual salary, title, and whether they are charged direct or indirect,

3. Detailed breakdown of the allocation base by cost element for each indirect cost rate,

4. Narrative explanation of the allocation base used for each indirect cost rate,

5. Reconciliation of the indirect cost and base cost used in the indirect rate calculation to the Financial Statements, and Statement of Functional Expenses if available,

6. A listing of all Federal awards and contracts identifying the following information:

   a. Total cost incurred for the fiscal year
   b. Period of performance
   c. Identification of any indirect cost limitations/ceilings
   d. Schedule of non-Federal awards as a reconciling item

7. For development of forecasted rates which differ from the actual rates for the most completed fiscal year, provide a narrative explanation of assumptions made to adjust historical cost, and

8. Explanation of any accounting system changes that occurred during the applicable period.

For an example of an adequate indirect cost rate proposal submission, see Appendix B of this guide.

B. Due Dates for Indirect Cost Proposal

The due dates for the submission of indirect cost proposals depends on whether the organization has an established indirect cost rate with the U.S. Government.

No Previous Rate Established

If an organization has yet to establish an indirect cost rate(s) with the U.S. Government, it should submit it's indirect cost rate proposal to the Government no later than three months after the award date. This proposal will form the basis for the negotiation of a provisional indirect cost rate(s) to allow funding of indirect costs under the award.

Previous Rate(s) Has Been Established

An organization that has an established indirect cost rate(s) with the U.S. Government, must submit it's indirect cost proposal within nine months of its fiscal year end (which is based on the expected revised due date for the A-133 audit). This proposal should be based on historical actual experience adjusted for known or expected significant deviations from actual experience.

Extension of Due Dates

If an organization believes it has extenuating circumstances which will prevent it from providing its indirect cost proposal on time, it should request an extension of the due date in writing from the Office of Overhead/Special Cost and Contract Closeout (OCC) Branch of USAID.

Where to submit

A copy of an organization's indirect cost proposal should be sent to:

James J. Deery, Branch Chief
M/OP/PS/OCC, Room No. 1433, SA-14
U.S. Agency for International Development
Washington, D.C. 20523-1417

Phone (703) 875-1101
FAX (703) 875-1027

Four copies of an organization's A-133 audit should be sent to:

Stephen Kroll, Branch Chief
M/OP/PS/CAM, Room 1425, SA-14
U.S. Agency for International Development
Washington, D.C. 20523-1416

Phone (703) 875-1825
FAX (703) 875-1027

SECTION I

EXAMPLES OF THE INDIRECT COST A CATION METHODS

In this section, we have provided examples of three allocation methods described in Attachment A, Section D of the OMB Circular A-122. fically, the examples provided are for the Simplified Allocation Method, the Direct Allocat ethod and the Special Indirect Cost Rate Method. We have not provided an example of Multiple Allocation Base Method because the criteria for it's use is rarely present with org ions that have awards or contracts with USAID.

Also included in the section is an illustration and disc of the treatment of fringe benefit cost.

SIMPLIFIED ALLOCATION METHOD

An example of the simplified allocation method, as defined in OMB Circular A-122, Section D.2 of Attachment A, is provided on Exhibits A and B on the following pages.

For purposes of this example, we are assuming that the organization's functions all benefit from indirect cost in relatively the same degree. Thus they choose the simplified allocation method to allocate cost. For further illustrative purposes, we have shown the rate development based on two different assumptions, depicted by Example A and B.

Example A assumes that it was determined that the allocation base should be Total Direct Cost Minus Medical Equipment. This base was chosen because the organization determined that the inclusion of Medical Equipment in the allocation base resulted in a significant distortion of the allocation of indirect cost. This is true because this organization incurs a significant amount of cost for a few high dollar pieces of medical equipment. In addition, the medical equipment purchased was delivered to its final destination by the supplier. Thus the organization did little more then pay for the medical equipment.

Example B assumes that an analysis was performed by the organization that determined a significant portion of the indirect cost had a strong relationship with the direct labor and fringe benefits expenses. Thus, an allocation base of total direct labor plus applicable fringe benefit cost was chosen to ensure an equitable distribution of indirect cost.

For further illustrative purposes, it is assumed that the organization incurred certain cost which were determined to be unallowable for Federal reimbursement in accordance with the cost principles contained in the OMB Circular A-122. Specifically, for this example, we assumed that they incurred cost related to Bad Debts, Interest and Entertainment, which are all deemed unallowable and thus not reimbursable on Federal awards per Attachment B of the OMB Circular A-122. Attachment B of A-122 provides the regulations regarding the allowability of selected cost items for Federal awards, and should be reviewed in its entirety before formal submission of an indirect cost rate proposal.

EXHIBIT A

SAMPLE SCHEDULE OF TOTAL COSTS
SIMPLIFIED ALLOCATION METHOD
JANUARY 1, 19XX TO DECEMBER 31, 19XX

	Total Costs	Less Unallowables & Exclusions	Note	Allowable Indirect Costs	Total Direct Costs
Salaries	$1,480,000			$450,000	$1,030,000
Fringe Benefits	414,400			126,000	288,400
Rent	180,000			180,000	0
Travel	78,000			8,500	69,500
Telephone	24,500			4,300	20,200
Print & Repro	37,800			6,500	31,300
Postage & Delivery	5,500			1,100	4,400
Depreciation	32,000			7,800	24,200
Bad Debts	4,000	4,000	1	0	0
Interest	2,700	2,700	1	0	0
Office Supplies	3,600			1,200	2,400
Dues/Membership	450			450	0
Insurance	35,000			35,000	0
Entertainment	2,700	2,700	1	0	0
Medical Equipment	1,000,000	1,000,000	2	0	0
Training Materials	32,000			0	32,000
Total	$3,332,650	$1,009,400		$820,850	$1,502,400

Notes

1. These cost are unallowable per the cost principles contained in Attachment B of the OMB Circular A-122.

2. For illustrative purposes, for example A, we are defining the allocation base as total direct cost minus medical equipment. Therefore, the cost of medical equipment is excluded from the allocation base for determining the applicable indirect cost rate.

EXHIBIT B

SAMPLE INDIRECT COST SCHEDULE
SIMPLIFIED ALLOCATION METHOD
JANUARY 1, 19XX TO DECEMBER 31, 19XX

	Cost Incurred	Less Unallowable Cost	Claimed Cost
Salaries	$450,000		$450,000
Fringe Benefits	126,000		126,000
Rent	180,000		180,000
Travel	8,500		8,500
Telephone	4,300		4,300
Printing & Repro.	6,500		6,500
Postage & Delivery	1,100		1,100
Depreciation	7,800		7,800
Bad Debts	4,000	4,000	0
Interest	2,700	2,700	0
Office Supplies	1,200		1,200
Dues/Membership	450		450
Insurance	35,000		35,000
Entertainment	2,700	2,700	0
Total	**$830,250**	**$9,400**	**$820,850**

Indirect Cost Rate Calculation

Example A		
Base = Total Direct Cost Minus Medical Equipment		
Pool Cost	$820,850	A
Base Cost	$1,502,400	B
Indirect Rate	54.64%	A/B

Example B			
Base = Direct Labor Plus Applicable Fringe Benefit Cost			
Pool Cost		$820,850	A
Base Cost Calculation			
Direct Labor	1,030,000		
Fringe	288,400		
Total Base		$1,318,400	B
Indirect Rate		62.26%	A/B

DIRECT ALLOCATION METHOD

An example of the direct allocation method, as defined in the OMB Circular A-122, Section D.4 of Attachment A, is provided on Exhibits C and D on the following pages.

For purposes of this example, we are assuming that the subject organization has determined it wishes to treat all cost as direct except for general administration and general expenses. Under this method, joint costs such as rental costs and telephone expenses are prorated individually as direct costs to each category and to each award or other activity using a base most appropriate to the particular cost being prorated. Examples of such allocation bases are provided in Exhibit E. For this example all of the indirect cost represent general administration and general expenses exclusively. For further illustrative purposes, we have shown the rate development based on two different assumptions, depicted by Example A and B.

Example A assumes that it was determined that the allocation base should be Total Direct Cost Minus Medical Equipment. This base was chosen because the organization determined that the inclusion of Medical Equipment in the allocation base resulted in a significant distortion of the allocation of indirect cost. This is true because this organization incurs a significant amount of cost for a few high dollar pieces of medical equipment. In addition, the medical equipment purchased was delivered to its final destination by the supplier. Thus the organization did little more then pay for the medical equipment.

Example B assumes that an analysis was performed by the organization that determined a significant portion of the indirect cost had a strong relationship with the direct labor and fringe benefits expenses. Thus, an allocation base of total direct labor plus applicable fringe benefit cost was chosen to ensure an equitable distribution of indirect cost

For further illustrative purposes, it is assumed that the organization incurred certain cost which were determined to be unallowable for Federal reimbursement in accordance with the cost principles contained in the OMB Circular A-122. Specifically, for this example, we assumed that they incurred cost related to Bad Debts, Interest and Entertainment, which are all deemed unallowable and thus not reimbursable on Federal awards per Attachment B of the OMB Circular A-122. Attachment B of A-122 provides the regulations regarding the allowability of selected cost items for Federal awards, and should be reviewed in its entirety before formal submission of an indirect cost rate proposal.

EXHIBIT C

SAMPLE SCHEDULE OF TOTAL COSTS
DIRECT ALLOCATION METHOD
JANUARY 1, 19XX TO DECEMBER 31, 19XX

	Total Costs	Less Unallowables & Exclusions	Note	Allowable Indirect Costs	Total Direct Costs	USAID Award A	USAID Award B	EPA Award A	Private Foundation	Fund Raising
Salaries	$1,480,000			$450,000	$1,030,000	$530,000	$187,000	$84,700	$220,000	$8,300
Fringe Benefits	414,400			126,000	288,400	148,400	52,360	23,716	61,600	2,324
Rent	180,000			35,000	145,000	74,612	26,325	11,924	31,039	1,100
Travel	78,000			8,500	69,500	36,322	12,618	5,715	14,845	0
Telephone	24,500			4,300	20,200	10,394	2,830	1,661	4,315	1,000
Print & Repro	37,800			6,500	31,300	16,106	4,935	2,574	6,685	1,000
Postage & Delivery	5,500			1,100	4,400	2,264	584	362	940	250
Depreciation	32,000			7,800	24,200	12,452	4,394	2,185	5,169	0
Bad Debts	4,000	4,000	1	0	0	0	0	0	0	0
Interest	2,700	2,700	1	0	0	0	0	0	0	0
Office Supplies	3,600			1,200	2,400	1,154	436	197	413	200
Dues/Membership	450			450	0	0	0	0	0	0
Insurance	35,000			2,500	32,500	16,723	5,900	2,673	6,942	262
Entertainment	2,700	2,700	1	0	0	0	0	0	0	0
Medical Equipment	1,000,000	1,000,000	2	0	0	0	0	0	0	0
Training Materials	32,000			0	32,000	16,466	5,810	2,889	6,835	0
Total	$3,332,650	$1,009,400		$643,350	$1,679,900	$864,893	$303,192	$138,596	$358,783	$14,436

Notes

1. These cost are unallowable per the cost principles contained in Attachment B of the OMB Circular A-122.

2. For illustrative purposes, for example A, we are defining the allocation base as total direct cost minus medical equipment. Therefore, the cost of medical equipment is excluded from the allocation base for determining the applicable indirect cost rate.

SAMPLE INDIRECT COST SCHEDULE
DIRECT ALLOCATION METHOD
JANUARY 1, 19XX TO DECEMBER 31, 19XX

	Indirect Cost Incurred	Less Unallowable Cost	Claimed Cost
Salaries	$450,000		$450,000
Fringe Benefits @ 28%	126,000		126,000
Rent	35,000		35,000
Travel	8,500		8,500
Telephone	4,300		4,300
Printing & Repro.	6,500		6,500
Postage & Delivery	1,100		1,100
Depreciation	7,800		7,800
Bad Debts	4,000	4,000	0
Interest	2,700	2,700	0
Office Supplies	1,200		1,200
Dues/Membership	450		450
Insurance	2,500		2,500
Entertainment	2,700	2,700	0
Total	$652,750	$9,400	$643,350

Indirect Cost Rate Calculation

Example A		
Base = Total Direct Cost Minus Medical Equipment		
Pool Cost	$643,350	A
Base Cost	$1,679,900	B
Indirect Rate	38.30%	A/B

Example B			
Base = Direct Labor Plus Applicable Fringe Benefit Cost			
Pool Cost		$643,350	A
Base Cost Calculation			
Direct Labor	1,030,000		
Fringe @ 28%	288,400		
Total Base		$1,318,400	B
Indirect Rate		48.80%	A/B

EXHIBIT E

SUGGESTED ALLOCATION BASES USED TO DIRECT CHARGE JOINT COSTS TO FEDERAL AWARDS

Cost Element	Allocation Base
Accounting	Number of transactions processed
Auditing	Direct audit hours
Automobile use	Miles driven or days used
Data processing	Jobs performed, hours used
Disbursing service	Number of checks or warrants issued
Equipment repair	Direct hours
Facilities cost (rent, utilities)	Square feet of space occupied
Health services	Number of employees
Insurance management service	Dollar value of insurance premiums
Legal services	Direct hours
Mail & messenger	Number of documents handled or people serviced
Payroll services	Number of employees
Personnel administration	Number of employees
Printing & reproduction	Number of pages printed, direct hours, number of jobs
Procurement service	Number of transactions processed
Telephone	Number of telephone instruments

SPECIAL INDIRECT COST RATES

An example of an application of a special indirect cost rate, as defined in the OMB Circular A-122, Section D.5 of Attachment A, is provided on Exhibits F and G on the following pages.

For purposes of this example, we are assuming that this organization has a home office in Atlanta, Georgia, and four offsite locations. Three of the offsite locations are in West Africa and support three awards each and are all for the same type of work, humanitarian assistance. Since all of these awards are: (i) for the same type of work, (ii) supported administratively by the Atlanta home office, and (iii) the cost involved are relatively minor and even among awards, they have created one overhead rate, the home overhead rate, to distribute applicable indirect cost to these nine awards.

The remaining offsite location is in South Africa and is in a facility being furnished free to the organization by the U.S Government. This offsite location was created to help the democracy movement in South Africa. This location also has a separate payroll system and its own accounting staff, separate from the Atlanta office. Since this offsite location: (i) is not supported by the Atlanta staff in any material way, (ii) is supported by its own accounting and administrative staff, (iii) is for a different line of work then the other offsite locations and (iv) has no rent cost, a separate offsite rate was developed, which is applicable only to those awards performed out of South Africa, i.e., USAID awards D through F.

For further illustrative purposes, it is assumed that the organization incurred certain cost which were determined to be unallowable for Federal reimbursement in accordance with the cost principles contained in the OMB Circular A-122. Specifically, for this example, we assumed that they incurred cost related to Bad Debts, Interest and Entertainment, which are all deemed unallowable and thus not reimbursable on Federal awards per Attachment B of the OMB Circular A-122. Attachment B of A-122 provides the regulations regarding the allowability of selected cost items for Federal awards, and should be reviewed in its entirety before formal submission of an indirect cost rate proposal.

EXHIBIT F

SAMPLE INDIRECT COST SCHEDULE
SPECIAL INDIRECT COST RATES
JANUARY 1, 19XX TO DECEMBER 31, 19XX

Indirect Cost	Incurred Home Overhead	Less Unallowables	Note	Claimed Home Overhead	Incurred Offsite Overhead	Less Unallowables	Note	Claim Offs Overh
Salaries	$450,000			$450,000	$1,234,543			$1,234
Fringe Benefits	126,000			126,000	432,090			432
Rent	180,000			180,000	0		2	
Travel	8,500			8,500	98,000			98
Accounting	14,000			14,000	32,345		3	32
Payroll Processing	4,800			4,800	10,000		3	10
Telephone	4,300			4,300	7,500			7
Printing & Repro.	6,500			6,500	8,000			8
Postage & Delivery	1,100			1,100	5,400			5
Depreciation	7,800			7,800	34,000			34
Bad Debts	1,300	1,300	1	0	0	0	1	
Interest	2,900	2,900	1	0	4,300	4,300	1	
Office Supplies	1,200			1,200	4,000			4,
Dues/Membership	450			450	300			
Entertainment	2,700	2,700	1	0	6,800	6,800	1	
Misc.	3,200			3,200	5,300			5
Total	**$811,550**	**$6,900**		**$804,650**	**$1,877,278**	**$11,100**		**$1,866**

Notes

1. These cost are considered unallowable for reimbursement on Federal awards in accordance with the cost principles contained in Attachment B of the OMB Circular A-122.

2. This organization has developed an offsite rate in Africa which is based out of a facility that is being paid for dire by the U.S. Government.

3. This offsite location has its own accounting staff and payroll processing.

SAMPLE INDIRECT COST RATE CALCULATION
SPECIAL INDIRECT COST RATES
JANUARY 1, 19XX TO DECEMBER 31, 19XX

Direct Cost	Home	Offsite
USAID Award A	$456,789	
USAID Award B	234,567	
USAID Award C	123,456	
USAID Award D		654,321
USAID Award E		765,432
USAID Award F		987,654
USAID Award G		456,654
USAID Award H		876,678
USAID Award I		987,786
USAID Award J		1,000,765
USAID Award K		456,786
USAID Award L		987,788
USAID Award M		345,345
USAID Award N	123,432	
USAID Award O	234,543	
USAID Award P	342,342	
USAID Award Q	344,333	
USAID Award R	123,221	
USAID Award S	213,111	
Total Direct Cost	$2,195,794	$7,519,209

Indirect Cost Rate Calculation

	Home Overhead Rate		Note
Pool Cost	$804,650	A	1
Base Cost	$2,195,794	B	2
Indirect Rate	36.65%	A/B	

	Offsite Rate		Note
Pool Cost	$1,866,178	A	1
Base Cost	$7,519,209	B	2
Indirect Rate	24.82%	A/B	

Note

1 The pool cost for the home and offsite overhead rates are detailed on Exhibit F on the preceding page.

2 The base cost applicable for both overhead rates are shown above.
The allocation base is total direct cost.
See notes at beginning of this section for further explanation.

FRINGE BENEFITS

Fringe Benefit expenses consist of the cost of paid absences such as vacation leave, sick leave, holiday leave and jury duty, and employer contributions such as social security, employee insurance, workmen's compensation insurance, and pension plan costs. For these costs to be allowable and allocable to Federal awards they must be absorbed by all organization activities in proportion to the relative amount of time or effort actually devoted to each and are granted in accordance with established written organization policies. Attachment B, Item 6.f. of the OMB Circular A-122 discusses the cost principles governing fringe benefit expenses.

Fringe benefit costs my be treated as either direct or indirect cost. To treat the cost as direct, an organization may identify all cost specifically applicable to each employee and allocate it on the same basis as the individual's salary or hourly wage, or they may allocate it based on a fringe benefit rate(s). Each individual type of fringe benefit cost (i.e., paid absences or pension) does not need to be treated in the same manner, as long as each type of fringe benefit is treated consistently. If the costs of benefits provided to groups of employees (executives, hourly employees) vary significantly in relation to the salaries and wages of employees in each group, then separate fringe benefit rates must be established for each group.

If the fringe benefit cost are to be treated as purely indirect cost, then the fringe benefit cost are not specifically identified to each employee, only groups of employees. The fringe cost applicable to each group of employees would be included in the overhead pool for the indirect cost rate that includes that group of employees labor cost in the allocation base. If an organization has only one indirect cost rate, all fringe benefit cost would simply be included in this overhead pool.

A fringe benefit indirect cost rate would be developed by dividing total fringe benefit cost by an equitable allocation base. Generally, the allocation base for fringe benefits is total salaries as most of the fringe benefit cost are tied to the cost of labor.

When an organization's indirect cost rate structure includes a fringe benefit rate and other indirect cost rates, then the fringe benefits applicable to indirect salaries would be included in the overhead cost pools by applying the fringe benefit rate to the indirect salaries included in the overhead pools.

When an organization uses it's fringe benefit rate for billing and bidding it takes on the characteristics of an indirect cost rate. The Office of Special/Overhead Costs and Contract Closeout (OCC) Branch will review and approve fringe benefit rates in the same manner it addresses other indirect rates. The approved fringe benefit rate will be incorporated into the Negotiated Indirect Cost Rate Agreement (NICRA).

To illustrate how fringe benefit cost can be allocated, example schedules have been developed and are shown on Exhibits H through L. For purposes of these examples we have made some assumptions which are explained on the next page.

For Exhibits H through J

The organization has decided to develop a fringe benefits rate with an allocation base of total labor cost. They also have an overhead rate. For further illustrative purposes we have developed the overhead rate based on two different allocation bases, depicted by Examples A and B.

Example A assumes that it was determined that the allocation base should be total direct cost.

Example B assumes that an analysis was performed by the organization that determined the majority of the indirect cost had a significant relationship with direct labor and fringe benefits. Thus, an allocation base of total direct labor plus applicable fringe benefit cost was chosen to ensure an equitable distribution of indirect cost.

For Exhibits K and L

The organization has decided not to develop a fringe benefits rate and simply put all fringe benefit cost into it's single overhead pool.

For all Exhibits

For further illustrative purposes, it is assumed that the organization incurred certain cost which were determined to be unallowable for Federal reimbursement in accordance with the cost principles contained in the OMB Circular A-122. Specifically, for this example, we assumed that they incurred cost related to Bad Debts, Interest and Entertainment, which are all deemed unallowable and thus not reimbursable on Federal awards per Attachment B of the OMB Circular A-122. Attachment B of A-122 provides the regulations regarding the allowability of selected cost items for Federal awards, and should be reviewed in its entirety before formal submission of an indirect cost rate proposal.

SAMPLE SCHEDULE OF TOTAL COSTS
WHEN A SEPARATE FRINGE BENEFIT RATE EXISTS
JANUARY 1, 19XX TO DECEMBER 31, 19XX

	Total Costs	Less Unallowables & Exclusions	Note	Allowable Indirect Costs	Total Direct Costs	USAID Award A	USAID Award B	EPA Award A	Private Foundation	Fund Raising
Salaries	$1,876,345			$450,000	$1,426,345	$702,000	$302,786	$184,700	$220,034	$16,825
Fringe Benefits	517,883			124,200	393,671	193,752	83,569	50,977	60,729	4,644
Rent	180,000			35,000	145,000	74,612	26,325	11,924	31,039	1,100
Travel	78,000			8,500	69,500	36,322	12,618	5,715	14,845	0
Telephone	24,500			4,300	20,200	10,394	2,830	1,661	4,315	1,000
Print & Repro	37,800			6,500	31,300	16,106	4,935	2,574	6,685	1,000
Postage & Delivery	5,500			1,100	4,400	2,264	584	362	940	250
Depreciation	32,000			7,800	24,200	12,452	4,394	2,185	5,169	0
Bad Debts	4,000	4,000	1	0	0	0	0	0	0	0
Interest	2,700	2,700	1	0	0	0	0	0	0	0
Office Supplies	3,600			1,200	2,400	1,154	436	197	413	200
Dues/Membership	450			450	0	0	0	0	0	0
Insurance	35,000			2,500	32,500	16,723	5,900	2,673	6,942	262
Entertainment	2,700	2,700	1	0	0	0	0	0	0	0
Training Materials	32,000			0	32,000	16,466	5,810	2,889	6,835	0
Total	$2,832,478	$9,400		$641,550	$2,181,516	$1,082,245	$450,187	$265,858	$357,946	$25,281

Allocation of Indirect Cost	Total	USAID Award A	USAID Award B	EPA Award A	Private Foundation	Fund Raising
Example A - Allocation base equals total direct cost and rate = 29.41%	641,550	318,271	132,393	78,185	105,266	7,435
Example B - Allocation base equals direct labor plus fringe and rate = 35.25%	641,550	315,750	136,189	83,075	98,968	7,568

The separate overhead rates are based on two different assumptions which are explained on the previous page. The individual indirect overhead rates are calculated on Exhibit J.

Notes

1. These cost are unallowable per the cost principles contained in Attachment B of the OMB Circular A-122.

EXHIBIT I

SCHEDULE OF FRINGE BENEFIT COST
JANUARY 1, 19XX TO DECEMBER 31, 19XX

Cost Element	Cost Incurred	
Vacation Leave Accrued	63,456	
Sick Leave	21,456	
Holidays	48,976	
FICA	123,000	
SUTA	21,342	
Workmens Compensation Insurance	15,432	
Medical Insurance	101,345	
Pension	122,876	
Total Fringe Benefits	$517,883	
Alocation Base		
Total Salaries	$1,876,345	Reconciles to Exhibit H
Fringe Benfit Rate	27.60%	

EXHIBIT J

SAMPLE INDIRECT COST SCHEDULE
WHEN THERE IS A SEPARATE FRINGE BENEFITS RATE
JANUARY 1, 19XX TO DECEMBER 31, 19XX

	Indirect Cost Incurred	Less Unallowable Cost	Claimed Cost	
Salaries	$450,000		$450,000	
Fringe Benefits @ 27.6%	124,200		124,200	Fringe Benefit rate is calculated on Exhibit I
Rent	35,000		35,000	
Travel	8,500		8,500	
Telephone	4,300		4,300	
Printing & Repro.	6,500		6,500	
Postage & Delivery	1,100		1,100	
Depreciation	7,800		7,800	
Bad Debts	4,000	4,000	0	
Interest	2,700	2,700	0	
Office Supplies	1,200		1,200	
Dues/Membership	450		450	
Insurance	2,500		2,500	
Entertainment	2,700	2,700	0	
Total	**$650,950**	**$9,400**	**$641,550**	

Indirect Cost Rate Calculation

Example A			
Base = Total Direct Cost			
Pool Cost	$641,550	A	
Base Cost	$2,181,516	B	Reconciles to Exhibit H
Indirect Rate	29.41%	A/B	

Example B				
Base = Direct Labor Plus Applicable Fringe Benefit Cost				
Pool Cost		$641,550	A	
Base Cost Calculation				
Direct Labor	1,426,345			Reconciles to Exhibit H
Fringe @ 27.6%	393,671			Reconciles to Exhibit H
Total Base		$1,820,016	B	
Indirect Rate		35.25%	A/B	

SAMPLE SCHEDULE OF TOTAL COSTS
WHEN THERE IS NO SEPARATE FRINGE BENEFITS RATE
JANUARY 1, 19XX TO DECEMBER 31, 19XX

	Total Costs	Less Unallowables & Exclusions	Note	Allowable Indirect Costs	Total Direct Costs	USAID Award A	USAID Award B	EPA Award A	Private Foundation	Fund Raising
Salaries	$1,876,345			$450,000	$1,426,345	$702,000	$302,786	$184,700	$220,034	$16,825
Fringe Benefits	517,883			517,883	0	0	0	0	0	0
Rent	180,000			35,000	145,000	74,612	26,325	11,924	31,039	1,100
Travel	78,000			8,500	69,500	36,322	12,618	5,715	14,845	0
Telephone	24,500			4,300	20,200	10,394	2,830	1,661	4,315	1,000
Print & Repro	37,800			6,500	31,300	16,106	4,935	2,574	6,685	1,000
Postage & Delivery	5,500			1,100	4,400	2,264	584	362	940	250
Depreciation	32,000			7,800	24,200	12,452	4,394	2,185	5,169	0
Bad Debts	4,000	4,000	1	0	0	0	0	0	0	0
Interest	2,700	2,700	1	0	0	0	0	0	0	0
Office Supplies	3,600			1,200	2,400	1,154	436	197	413	200
Dues/Membership	450			450	0	0	0	0	0	0
Insurance	35,000			2,500	32,500	16,723	5,900	2,673	6,942	262
Entertainment	2,700	2,700	1	0	0	0	0	0	0	0
Training Materials	32,000			0	32,000	16,466	5,810	2,889	6,835	0
Total	$2,832,478	$9,400		$1,035,233	$1,787,845	$888,493	$366,618	$214,880	$297,217	$20,637

Allocation of Indirect Cost	Total	USAID Award A	USAID Award B	EPA Award A	Private Foundation	Fund Raising
Allocation base equals total direct cost and the rate = 57.90%	$1,035,233	$514,473	$212,286	$124,424	$172,100	$11,950

The overhead rate is calculated on Exhibit L and is based on the assumption that the organization has no separate fringe benefits rate.

Notes

1. These cost are unallowable per the cost principles contained in Attachment B of the OMB Circular A-122.

EXHIBIT L

SAMPLE INDIRECT COST SCHEDULE
WHEN NO SEPARATE FRINGE BENEFITS RATE EXISTS
JANUARY 1, 19XX TO DECEMBER 31, 19XX

	Indirect Cost Incurred	Less Unallowable Cost	Claimed Cost
Salaries	$450,000		$450,000
Fringe Benefits	517,883		517,883
Rent	35,000		35,000
Travel	8,500		8,500
Telephone	4,300		4,300
Printing & Repro.	6,500		6,500
Postage & Delivery	1,100		1,100
Depreciation	7,800		7,800
Bad Debts	4,000	4,000	0
Interest	2,700	2,700	0
Office Supplies	1,200		1,200
Dues/Membership	450		450
Insurance	2,500		2,500
Entertainment	2,700	2,700	0
Total	$1,044,633	$9,400	$1,035,233

Indirect Cost Rate Calculation			
Example A			
Base = Total Direct Cost			
Pool Cost	$1,035,233	A	
Base Cost	$1,787,845	B	Reconciles to Exhibit K
Indirect Rate	57.90%	A/B	

SECTION V

Identification of Problem Areas

In this section, a few common problem areas as identified by the USAID IG, Contract Audit Management Branch (CAM), and the Office of Overhead/Special Costs and Contract Closeout Branch (OCC) are discussed. These deficiencies seem to indicate an insufficient understanding of the applicable Federal regulations and cost principles. Accordingly, we are providing this guidance in hopes of improving the comprehension of the subject regulations and cost principles. The topics covered are as follows:

1. Claiming Unallowable Cost for Reimbursement

2. Indirect Cost Allocation Bases

3. Changing of the Indirect Cost Rate Structure Without Prior Approval From USAID Officials

4. Timekeeping Systems

5. Subrecipient Audits

1. <u>Claiming Unallowable Cost for Reimbursement</u>

Certain cost are deemed by the U.S. Government to be unallowable for reimbursement on U.S. Government awards and contracts. For nonprofit organizations, Attachment B of the OMB Circular A-122, "Cost Principles for Nonprofit Organizations," covers the allowability of selected areas of cost. It is the organization's responsibility to directly identify unallowable cost upon cost incurrence and segregate and classify these cost as unallowable. This helps ensures that these cost will not be claimed on subsequent Government billing as either a direct cost or as an indirect cost through the indirect cost rate. Generally, an efficient organization will establish separate account numbers to identify and track unallowable cost.

Some cost are "expressly unallowable" and thus should never be claimed for reimbursement on Federal awards. Excerpts of these "expressly unallowable" cost as defined in Attachment B of OMB Circular A-122 are shown below. The numbers to the left of the cost title correspond to the numbering sequence of Attachment B.

"2. <u>Bad Debts.</u> Bad debts, including losses (whether actual or estimated) arising from uncollectible accounts and other claims, related collection costs and related legal cost are unallowable."

"7. Contingency provisions. Contributions to a contingency reserve or any similar provision made for events the occurrence of which cannot be foretold with certainty as to time, intensity, or with an assurance of their happening, are unallowable."

"8. Contributions. Contributions and donations by the organization to others are unallowable."

"12. Entertainment costs. Costs of amusement, diversion, social activities, ceremonies, and costs relating thereto, such as meals, lodging, rentals transportation, and gratuities are unallowable...."

"19. Interest, fund raising, and investment management costs.

a. Costs incurred for interest on borrowed capital or temporary use of endowment funds, however, represented are unallowable.

b. Costs of organized fund raising, including financial campaigns, endowment drives, solicitation of gifts and bequests, and similar expenses incurred solely to raise capital or obtain contributions are unallowable.

c. Costs of investment counsel and staff and similar expenses incurred solely to enhance income from investments are unallowable."

"21. Lobbying.

a. Notwithstanding other provisions of this Circular, costs associated with the following activities (for example, establishing, administering, contributing to, or paying the expenses of, a political party, campaign, political action committee, etc., and attempt to influence the enactment or modification of any pending Federal legislation through communication with any member or employee of the Congress) are unallowable."

"35. Professional service cost.

d. Costs of legal, accounting, and consulting services, and related costs incurred in connection with defense in antitrust suits, and the prosecution of claims against the Government are unallowable."

"37. Public information service costs.

b. Public information service costs are allowable as direct costs with prior approval of the awarding agency. Such costs are unallowable as indirect costs."

The problem encountered by USAID officials regarding unal. ble cost is that organizations are not fully aware of these cost principles and thus are claim: eimbursement for cost which are not reimbursable per the cost principles contained in th MB Circular A-122. ..Thus, organizations need to educate their employees on cost allov ity criteria contained in the subject circular. Extra special care should be given when paring the indirect cost rate proposal, to ensure all unallowable cost have been excluded f the indirect cost pools.

2. . <u>Indirect Cost Allocation Base</u>

Many organization have chosen indirect cost allocatior es which do not result in an equitable distribution of indirect cost to final cost object: It is imperative that an organization put careful thought into the development of its in t allocation bases. The most common problems identified with indirect cost allocation ba: nvolve: (i) the choice of an inequitable allocation base, (ii) the exclusion of some awards racts or cost activities from the allocation of indirect cost, and (iii) the exclusion of unal ble cost from the allocation base.

An organization must continuously evaluate whether the alloca: of its indirect cost to its final cost objectives mirrors the benefits received that these final objectives receive from the indirect cost activities being allocated. Attachment A, Paragr: 4.a of the OMB Circular A-122, states that "A cost is allocable to a particular cost obj e, such as a grant/contract, project, service, or other activity, in accordance with the rela benefits received." The key here is "relative benefits received." Accounting is not a perfe ience and thus the goal is to develop an allocation base which allocates indirect cost to final objectives, in a relationship that approximates the relative benefits received. Since indirect by their very nature are not directly identifiable to any one final cost objective, the ir t relationship needs to be identified. Paragraph D.2.c of OMB Circular A-122 provide ne guidance as to generally accepted indirect cost allocation bases by stating: "The distr on base may be total direct costs (excluding capital expenditures and other distorting item ch as major subcontracts or subgrants), direct salaries and wages or other bases which resu a an equitable distribution." The fact that they specifically identify total direct cost and dir salaries as examples implies that these bases generally result in an equitable distribution of . And, in fact, the majority of USAID grantees/contractors appropriately utilize one of thes ses. However, the specifics of each organization need to be evaluated before an allocati ase is chosen. One of the problems USAID has encountered involves organizations who e to exclude items from the allocation base, which in fact are generating indirect cost in r or less the same amount as other items which are in the allocation base. Thus, by exclu these items from the base, some awards/contracts are not getting their fair share of i ct cost allocated to them. Conversely, some organizations are including cost items in t location base which do not generate cost in the same proportion as other cost in the allo n base, and thus should be excluded. Such items tend to be high dollar activities which req little management, oversight or support. The use of an inequitable allocation base may resu questioned cost.

For an allocation base to be acceptable it must be capable of allocating indirect cost equitably to **all** awards and contracts. The fact that a certain award or contract has an indirect cost limitation should have no bearing on it's **allocation** of cost for purposes of determining actual cost incurred, and reporting of these costs for financial reporting. These indirect cost limitations only apply to the amount reimbursable by the Government. Thus, if an organization has an award that does not allow indirect cost as a reimbursable cost, and the allocation base for the organization's indirect cost rate is defined as total direct cost, this award would nonetheless require the allocation of indirect cost. However, these cost must be excluded from any amounts billed. The same principle applies if an award has a ceiling limitation on it's indirect cost rate which is lower then the determined actual rate for the period. In this instance, the full share of indirect costs must be allocated to this award, and the amount billed will be limited to the ceiling limitation. This is true, because Attachment A, of the OMB Circular A-122 provides that any costs allocable to other cost objectives may not be shifted to a Federal award to "overcome funding deficiencies."

Similarly, all cost which normally would be in the allocation base, remain in the allocation base whether deemed allowable or unallowable by the criteria in the OMB Circular A-122, so that they can bear their pro rata share of indirect cost. Thus, for example, although fund raising cost are deemed unallowable as a reimbursable cost for Government awards, they are nonetheless included in the allocation base for the distribution of indirect cost.

3. Changing of the Indirect Cost Rate Structure Without Prior Approval From USAID Officials

Prior approval from the Office of Overhead/Special Costs and Contract Closeout Branch (OCC) of USAID must be obtained before an organization can change the way it allocates cost. Once an organization has awards and contracts with USAID based on an accepted established indirect cost rate structure, agreement has been reached on how cost are to be allocated to awards/contracts. Accordingly, any modification of the allocation methodology constitutes a change in these agreements and thus requires prior approval from USAID. Failure to obtain approval may result in cost disallowances.

More on this issue is presented in Section II C. of this guide.

4. Timekeeping Systems

Since the majority of organizations doing business with USAID are labor intensive, USAID has considerable interest in the propriety of an organization's timekeeping system. It has become apparent that many organizations do not effectively account for labor effort and it's corresponding cost. USAID has questioned substantial amounts of labor cost due to deficient timekeeping procedures. Often, these organizations had no real method of allocating labor cost to final cost objects.

Guidance regarding the attributes of an acceptable timekeeping system are contained in Attachment B, Paragraph 6 of the OMB Circular A-122. This section states that compensation cost, whether treated as direct or indirect costs, will be based on documented payrolls. In addition, the distribution of this compensation expense to final cost objectives must be supported by personnel activity reports (timesheets). It explains that the labor reports must reflect "an after-the-fact determination of the actual activity of each employee." That is, labor reports must be based on how employees actually spent their time. Estimates do not qualify as support for charges to awards/contracts. In addition, these reports must be prepared at least monthly and coincide with one or more pay periods.

5. <u>Subrecipient Audit</u>

Under the requirements of OMB Circular A-133, prime recipients have a responsibility to ensure that Federal awards passed through to subrecipients are expended in accordance with Federal laws and regulations. Specifically the prime recipient auditor's responsibilities are to determine whether:

- The prime recipient's accounting system is adequate for monitoring subrecipients and obtaining and acting on subrecipient audit reports;

- The subrecipient has complied with A-128 or A-133 audit requirements, as applicable, and subrecipient audit reports are current; and

- Subrecipient questioned costs or compliance findings which may be material or otherwise require adjustment of the prime recipient records are properly reflected by the prime recipient.

The USAID has experienced a high number of organizations who have completed their A-133 audit without obtaining the required A-133 audits for applicable subrecipients. The prime recipient is required to ensure that subrecipients to whom it provides $25,000 (expected to increase with the revised Circular) or more in Federal awards meet applicable audit requirements. Possible consequences for lack of subrecipient audits are modifications to the prime recipient's audit reports, disallowed costs, or other adverse actions by Federal agencies.

An alternative when a prime recipient is unable to obtain a subrecipient audit is to expand the their audit to include testing of subrecipient records for compliance. Even though the expanded testing could permit a clean prime recipient audit opinion and show proper accountability for Federal awards, there would still be a compliance finding for lack of subrecipient audits.

Under the proposed changes to the OMB Circular A-133, the Circular will not apply to <u>non-U.S. based entities</u> receiving Federal awards either directly as a recipient or indirectly as a subrecipient. However, this does not negate the responsibility of the prime recipient to ensure Federal awards passed through to non-U.S. based subrecipients are expended in accordance with Federal laws and regulations.

APPENDIX A

EXAMPLE OF A NEGOTIATED INDIRECT COST RATE AGREEMENT (NICRA)

SAMPLE

Mr. John Doe
Vice President, Finance & Administration
International Nonprofit Organization
1111 11th Street, S.W.
Washington, D.C. 20036

Subject: Negotiated Indirect Cost Rate Agreement (NICRA)

Dear Mr. Doe:

The Overhead and Special Costs and Contract Closeout Branch of the Office of Procurement is the central unit authorized to negotiate indirect cost rates with concerns awarded contracts, grants, or cooperative agreements by the U.S. Agency for International Development (USAID).

Enclosed is the USAID NICRA for execution by the appropriate official in your organization. This NICRA establishes the negotiated final indirect cost rates for the fiscal years ending June 30, 1992 and 1993 and the provisional indirect cost rate for the period July 1, 1993 until amended. Pursuant to AIDAR 742.770, these indirect cost rates are automatically incorporated into the awards shown in Part III of this agreement.

Please sign the original and the two copies of the NICRA. Retain one copy and return the original and one copy as soon as possible to me. For contracts, grants, or cooperative agreements which incorporate these rates, take the necessary actions to adjust your invoices for the difference between the billed and the indirect cost rates reflected in the NICRA. However, these negotiated rates shall not change any monetary ceiling, obligation, or specific cost allowance or disallowance provided for in each award between the parties.

Your expeditious return of the signed documents will be appreciated. Should you have any questions, please contact Steve Tashjian on (703) 875-1101.

Sincerely yours,

James J. Deery
Chief, Overhead and Special Costs
and Contract Closeout Branch
Procurement Support Division
Office of Procurement

Enclosure: USAID Negotiated Indirect Cost Rate Agreement (NICRA)

SAMPLE

NEGOTIATED INDIRECT COST RATE AGREEMENT

Date: January XX, 1995

SUBJECT: Indirect Cost Rates for Use in Cost Reimbursement Type Agreements With the U.S. Agency for International Development (USAID)

REFERENCE: CAM Audit Report No. C-01-5-B-1111

CONTRACTOR or GRANTEE: International Nonprofit Organization
1111 11th Street, S.W.
Washington, D.C. 20036

PART I- NEGOTIATED INDIRECT COST RATES (%)

TYPE	EFFECTIVE PERIOD		INDIRECT COST		
	FROM	THROUGH	FRINGE BENEFITS (a)	OVERHEAD (b)	G&A (c)
Final	07-01-91	06-30-92	27.03%	32.1%	12.4%
Final	07-01-92	06-30-93	26.89%	34.2%	13.3%
Provisional	07-01-93	06-30-94	27.90%	30.2%	12.5%
Provisional	07-01-94	Until Amended	27.90%	30.2%	12.5%

<u>Base of Application</u>
a) Total Labor Dollars
b) Total Direct Labor Plus Applicable Fringe Benefit Cost
c) Total Cost Incurred Excluding G&A Cost

Acceptance of the rate(s) agreed to herein is predicated upon the conditions: (1) that no costs other than those incurred by the grantee/contractor were included in its indirect cost rate proposal and that such costs are legal obligations of the grantee/contractor; (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 the basis for acceptance of the rate(s) agreed to herein is not subsequently found to be materially incomplete or inaccurate.

AID 1420-47 (8-80) (See Reverse)

PART II - ITEMS NORMALLY TREATED AS DIRECT COSTS

PART III - SPECIAL TERMS AND CONDITIONS

Pursuant to § 742.770 of the Agency for International Development Acquisition Regulations (AIDAR), the negotiated indirect cost rates set forth in Part I of this Agreement are incorporated into USAID Agreements shown below. This agreement shall not change any monetary ceiling, obligation, or specific cost allowance or disallowance provided for in the Contracts or Grants listed below or any other Agreement between the parties.

Contract/Grant Number
USAID AWARD A
USAID AWARD B
USAID AWARD C

ACCEPTED: International Nonprofit Organization

BY ______________________

____
Printed or Typed Name

____
Title

____
Date

James J. Deery
CONTRACTING OFFICER /sat/
Overhead and Special Costs Branch
Procurement Support Division
Office of Procurement
U.S. Agency for International Development

DISTRIBUTION:

IG/A/FA
USAID NIAMEY
M/FM/CMP
USAID BAMAKO

AID 1420-47 (8-80) back

APPENDIX B

SAMPLE INDIRECT COST RATE PROPOSAL

SAMPLE INDIRECT COST RATE PROPOSAL

For illustrative purposes a sample indirect cost rate proposal is provided on the following pages. This organization is assumed to have an indirect rate structure consisting of a fringe benefits rate and an overhead rate. The allocation base for fringe benefits is total salaries and the allocation base for overhead is total direct cost. A listing of the Federal awards and contracts was not provided for purposes of this example, but should be provided in an actual submission. The Schedule of Federal Awards that is included as part of the A-133 audit would fulfill this requirement, if it is available.

NONPROFIT ORGANIZATION, INC

SCHEDULE OF TOTAL COSTS
JANUARY 1, 19XX TO DECEMBER 31, 19XX

	Total Costs	Less Unallowables & Exclusions	Note	Allowable Indirect Costs	Total Direct Costs	USAID Award A	USAID Award B	EPA Award A	Private Foundation	Fund Raising
Salaries	$1,876,345			$450,000	$1,426,345	$702,000	$302,786	$184,700	$220,034	$16,825
Fringe Benefits	517,883			124,200	393,671	193,752	83,569	50,977	60,729	4,644
Rent	180,000			35,000	145,000	74,612	26,325	11,924	31,039	1,100
Travel	78,000			8,500	69,500	36,322	12,618	5,715	14,845	0
Telephone	24,500			4,300	20,200	10,394	2,830	1,661	4,315	1,000
Print & Repro	37,800			6,500	31,300	16,106	4,935	2,574	6,685	1,000
Postage & Delivery	5,500			1,100	4,400	2,264	584	362	940	250
Depreciation	32,000			7,800	24,200	12,452	4,394	2,185	5,169	0
Bad Debts	4,000	4,000	1	0	0	0	0	0	0	0
Interest	2,700	2,700	1	0	0	0	0	0	0	0
Office Supplies	3,600			1,200	2,400	1,154	436	197	413	200
Dues/Membership	450			450	0	0	0	0	0	0
Insurance	35,000			2,500	32,500	16,723	5,900	2,673	6,942	262
Entertainment	2,700	2,700	1	0	0	0	0	0	0	0
Training Materials	32,000			0	32,000	16,466	5,810	2,889	6,835	0
Total	$2,832,478	$9,400		$641,550	$2,181,516	$1,082,245	$450,187	$265,858	$357,946	$25,281

	Total	USAID Award A	USAID Award B	EPA Award A	Private Foundation	Fund Raising
Allocation of Overhead at 29.41%	641,550	318,271	132,393	78,185	105,266	7,435

See accompanying schedule for the calculation of the indirect cost rate

Notes
1. These cost are unallowable per the cost principles contained in Attachment B of the OMB Circular A-122.

THIS SCHEDULE SHOULD RECONCILE TO THE FINANCIAL STATEMENTS AND STATEMENT OF FUNCTIONAL EXPENSES INCLUDED WITH THE A-133 AUDIT. IF THE NUMBERS DO NOT RECONCILE DIRECTLY, A SCHEDULE RECONCILING THE AMOUNTS SHOULD BE PREPARED.

NONPROFIT ORGANIZATION, INC.

SCHEDULE OF FRINGE BENEFIT COST
JANUARY 1, 19XX TO DECEMBER 31, 19XX

Cost Element	Cost Incurred	
Vacation Leave Accrued	63,456	
Sick Leave	21,456	
Holidays	48,976	
FICA	123,000	
SUTA	21,342	
Workmens Compensation Insurance	15,432	
Medical Insurance	101,345	
Pension	122,876	
Total Fringe Benefits	$517,883	
Alocation Base		
Total Salaries	$1,876,345	Reconciles to Schedule of Total Cost
Fringe Benfit Rate	27.60%	

NONPROFIT ORGANIZATION, INC.

SCHEDULE OF INDIRECT COST
JANUARY 1, 19XX TO DECEMBER 31, 19XX

	Indirect Cost Incurred	Less Unallowable Cost	Claimed Cost	Note
Salaries	$450,000		$450,000	
Fringe Benefits @ 27.6%	124,200		124,200	
Rent	35,000		35,000	
Travel	8,500		8,500	
Telephone	4,300		4,300	
Printing & Repro.	6,500		6,500	
Postage & Delivery	1,100		1,100	
Depreciation	7,800		7,800	
Bad Debts	4,000	4,000	0	1
Interest	2,700	2,700	0	1
Office Supplies	1,200		1,200	
Dues/Membership	450		450	
Insurance	2,500		2,500	
Entertainment	2,700	2,700	0	1
Total	$650,950	$9,400	$641,550	

Indirect Cost Rate Calculation

Base = Total Direct Cost			Note
Pool Cost	$641,550	A	2
Base Cost	$2,181,516	B	2
Indirect Rate	29.41%	A/B	

Notes

1. These cost are unallowable per the cost principles contained in Attachment B of the OMB Circular A-122.

2. These cost reconcile to the Schedule of Total Cost.

NONPROFIT ORGANIZATION, INC.
SCHEDULE OF EMPLOYEE'S SALARIES

FOR THE YEAR ENDED DECEMBER 31, 19XX

Employee	Title	Annual Salary	Direct or Indirect
Ahmuty, Andy D.	Program Manager	64,000	Both
Boss, James, B.	President	$123,000	Indirect
Comer, Barbara C.	Analyst	39,400	Direct
Jones, Lisa C.	Vice President	89,000	Indirect
Lister, Mary K.	Program Manager	78,000	Both
Money, Steve A.	Controller	75,000	Indirect
Rawdon, Brian, R.	Writer	36,500	Direct
Technical, John B.	Sr. Engineer	73,000	Direct
Thomas, Bryant L.	Jr. Engineer	64,300	Direct
Welsh, Janice E.	Jr. Engineer	65,000	Direct
Wiser, Cynthia B.	Secretary	26,700	Indirect
etc. etc. see note below			

We have only included a portion of this schedule to demonstrate it's format. The actual schedule to be submitted should include all employees of the organization. If an organization already has separate reports which together provide the data above, they can submit these separate reports in lieu of creating a new one to provide the required data.

FA WORKSHOP
Part VIII.A - CASE STUDY - Solution

ABC Foundation
INDIRECT COST SCHEDULE
Jan. 1, 2001 to December 31, 2001

	Costs Incurred	Unallowable Costs	Allowable Costs
Salaries	450,000	-	450,000
Fringe Benefits	126,000	-	126,000
Rent	180,000	-	180,000
Travel	10,500	-	10,500
Telephone	4,300	-	4,300
Print & Reproduction	6,500	-	6,500
Postage & Delivery	1,100	-	1,100
Depreciation	7,800	-	7,800
Bad Debts	5,500	5,500	-
Interest	8,000	8,000	-
Office Supplies	1,200	-	1,200
Donations	3,000	3,000	
Dues/Membership	450	-	450
Insurance	35,000	-	35,000
Entertainment	4,700	4,700	-
Total	**844,050**	**21,200**	**822,850**

Base = Direct Labor + Applicable Fringe Benefit Cost

Indirect Cost rate = $\dfrac{\text{Indirect Cost Pool}}{\text{Direct Labor + Fringe}}$

$$\frac{822{,}850}{1{,}318{,}400}$$

Indirect Cost rate = $\boxed{\textbf{62\%}}$

Since the calculated rate as presented above is only **62%**, ABC's proposed rate of 64% is **NOT** reasonable and acceptable.