

Webinar 2- Core Principles of Cost Allocations

PRESENTER: Welcome to this webinar on the core principles of cost allocation, presented by the US Department of Housing and Urban Development. Many of the ideas we will talk about today are applicable to all HUD programs. Primary audience is grantees and subrecipients of five multifamily housing grant programs-- Assisted Living Conversion Program, Congregate Housing Services Program, Section 811 Project Rental Assistance, Service Coordinators in Multifamily Housing, and Support Services Demonstration for Elderly Households in HUD-Assisted Multifamily Housing.

Our primary objective in this webinar is to help assure that grantees and subrecipients are able to safeguard grant funds and ensure that all funds are used for the purposes for which they were awarded. This toolkit provides straightforward statements of compliance and responsibilities, along with references to the underlying rules, regulations, and legislation that affect the financial and administrative management of multifamily housing grant awards.

Our primary objectives in today's presentation are five-fold. First, we wish to communicate the information clearly. Second is to define common technical terms to facilitate understanding and discussion. We also want to increase understanding of federal cost principles and their implementation in day-to-day program activities.

This webinar will provide descriptions and examples of direct and indirect costs and how to prove cost allocation methodologies. Ultimately, we hope that this presentation will stimulate additional questions. We will give you information at the end on how to find more online training opportunities. And of course, we want to build everyone's capacity for critical thinking.

Our primary objective is to help assure that grantees and subrecipients are able to safeguard funds and ensure that all funds are used for the purposes for which they were awarded. Let's begin by defining direct and indirect costs.

This diagram shows two colors, red at the top and blue at the bottom. Direct costs are those that can be specifically identified with a particular award or activity relatively easily and with a high degree of accuracy-- that is, costs that are related to performing activities for the HUD objectives. Indirect costs are serving common or joint objectives that benefit the organization as a whole.

What are direct costs? Identification with the federal award rather than the nature of the goods and services involved is the determining factor in distinguishing direct from indirect costs for federal award purposes. Examples of direct costs include the salaries and benefits paid to a case manager or services coordinator, time spent qualifying client for services for which they are eligible. And another example would be mileage reimbursement for staff making home visits.

Examples of indirect costs include rent, utilities, insurance, maintenance, and other expenditures related to shared space-- these might be considered facilities costs-- administrative and executive team functions that support multiple program areas, and then the purchaser's transportation costs and staff expenses that benefit multiple program areas.

Due to the diverse characteristics and accounting practices of nonprofit organizations, it is not possible to specify the types of costs that may be classified as indirect in all situations. One thing to remember, however, is that a cost may not be allocated as an indirect cost in one program if any similar costs have been assigned as a direct cost either in that specific program or within any program in the organization.

Essential to spending the federal funds correctly is understanding what is cost allocation. We define cost allocation as charging an expenditure, in part or as a whole, to a particular contract or project. All expenditures must be fully allocated 100% to one or more cost centers, or you might consider these as program areas.

Cost allocation is charging a cost or expenditure, in part or as a whole, to a particular contract or project. All expenditures must be fully allocated, 100%, either in one activity area or across multiple areas.

Each cost incurred for the same purpose must be treated consistently in similar circumstances. That is, it must be either a direct cost consistently or an indirect cost consistently. And it's always important to remember that federal cost allocation guidelines apply to all expenditures across the agency budget, not just for the HUD program.

Let's talk about a cost allocation plan. Costs that are shared between programs within agency must be allocated to those programs in accordance with their relative benefits, agency policies, and also generally accepted accounting principles. Later on, we'll talk more about 2 CFR Part 200, which guides the accounting for all federal expenses. Subpart 405 describes the principles that should be applied when dividing up shared costs.

Different class types may be divided using different methods, which should be, first of all, spelled out clearly, reasonable for the cost type and program environment in which the agency is operating, and followed consistently. In addition, we suggest that these cost allocation guidelines be reassessed annually as part of the agency's budget development process, because as costs change, the allocation plan may also change.

When we talk about administrative costs for HUD purposes, there are specific definitions. Because HUD programs have specific limits on the amounts of funds spent on grant administration, separating program costs from administrative costs is essential for financial management compliance.

Administrative costs in general include overall program management, budgeting, coordination, monitoring, reporting, and evaluation. This includes the salaries and benefits for personnel engaged in these activities as well as the cost of administrative services performed under third-party contractor agreements, including such activities as general legal services, accounting services, and financial audits.

It can also include the cost of goods and services required for program administration, including the rental or purchase of equipment, insurance, utilities, office supplies, and the rental and maintenance, but never the purchase, of office space.

We also wanted to talk briefly about the method for allocating indirect costs. 2 CFR Part 200, Subpart 414 described several acceptable methods for allocating indirect costs through federal grant awards.

First of all, most governmental entities-- so cities and states and counties-- and major nonprofit organizations will already have a negotiated, federally approved indirect cost rate. This rate must be approved by what's called the cognizant agency, which for the Department of Housing and Urban Development is, in fact, the US Department of Health and Human Services.

For those entities that do not have such a federally approved indirect cost rate, Appendix 4 to Part 200 lays out two other methods that grantees and their recipients are encouraged to employ. First, is the simplified allocation method, and second the direct allocation method.

To use the simplified allocation method, the major functions of an organization must benefit to approximately the same degree across the entity's activities. Or it can be employed when an organization has only one major function with a number of individual projects and activities.

For example, if the entity is just providing housing, and there are a number of different housing projects, then the simplified allocation method might work. But if the entity provides housing as well as support services, and operates a medical clinic and a food bank, then that would not be possible. This simplified allocation method may also be used when the level of federal funding is relatively small compared to the overall agency budget. When using the simplified allocation method, method.

Using direct allocation, we have the direct charging of administrative and clerical staff salaries. And this is appropriate if all four of the following conditions are met.

First of all, the administrative or clerical services are integral to the project or activity. Second, the individuals involved can be specifically identified with that project or activity. And typically, we would look to identify those staff members through their job descriptions as well as through their timesheets or other methods of recording their activity.

Third, such costs are explicitly included in the budget or have the prior written approval of the federal awarding agency. And finally, these costs are not also being recovered as indirect costs. Each cost must be pro-rated using a base that accurately measures the benefit provided to each federal award or other activity. The basis must be established in accordance with reasonable criteria and be supported by current data. Further, they should be in compliance with generally accepted accounting principles.

Using this method, all costs are limited to three categories-- program activities, including those paid for by federal grants, management functions and general expenses, which we call management in general, or M&G, and fundraising, which under the OMB regulations is never eligible for HUD reimbursement. OMB here stands for the Office of Management and Budget.

The prorated indirect costs are treated as if they were direct costs and are assigned to one of the categories above using an allocation strategy appropriate to each particular cost type. Detailed

instructions for implementing an item-by-item methodology are contained in the grantee's cost allocation plan.

This concludes our brief presentation of information on cost allocation. The final slide will indicate some additional resources that you can find on the HUD Exchange website, both on cost allocation as well as on other topics within the financial management and accounting sector. Thank you very much for your participation.