Final Transcript

HUD-US DEPT. OF HOUSING & URBAN DEVELOPMENT: Understanding Indirect Rates

June 12, 2018/2:00 p.m. EDT

SPEAKERS

Robin Booth

PRESENTATION

Moderator: Ladies and gentlemen, thank you for standing by. Welcome to the Understanding Indirect Rates Conference call. At this time, all participants are in a listen-only mode. [Operator instructions]. As a reminder, this conference is being recorded.

I would now like to turn the conference over to Robin Booth. Please go ahead.

Robin Good afternoon, and welcome to Understanding Indirect Rates, 10% de minimis and at-cost allocation plans. This is sponsored by the US Department of Housing & Urban Development Office of Housing Counseling.

Just want to go over some logistics for everyone that has called in, or want to ask questions, or want to find out how to get this presentation after it's completed. This is being recorded, and a playback number along with any other presentation materials, handouts, and transcripts will be actually emailed to you after the webinar, at least the playback number along with the presentation. It'll also be available on HUD Exchange.

I saw one person indicate they could not download the presentation, so if you can't get it now for whatever reasons, it will be available on HUD Exchange as well usually within two business days after the webinar. Your lines have been muted during the presentation, and we will not be taking live questions due to the number of participants. The handouts, if you didn't them prior to the webinar, maybe because you didn't register.

If you registered you should have received the handouts prior to the webinar. In addition you should be able to download them from your

control panel for this webinar. There should be a PDF file with the name of this training, and you should be able to download. As I said, if you cannot download those for any reasons, this presentation, along with any handouts, and the transcript, and audio will be available on HUD Exchange.

Within the next one to two business days, you will receive a thank you email. It indicates that this is your certificate of training. It will not be an attachment. The body of the email itself represents the certificate so you should download or save that information and keep it for your records to verify training.

For this particular webinar, due to the large number of participants, we will not be taking live questions; however, we do have staff on standby that are prepared to respond to any questions that you submit through your control panel for this webinar. You can actually go to questions, enter your question, and you should receive a response from one of our staff members that are on standby reviewing, and accepting, and responding to questions.

In addition, if after this presentation you have some additional questions, you can always send them to housing.counseling@hud.gov. We ask that you put Understanding Indirect Rates in the subject line item so that your question can be properly distributed to the individual best able to respond. You can ask questions during the presentation; they'll just have to be through your control panel.

After this webinar, you will receive a brief survey. You'll be asked to complete the survey, and we'd really appreciate it if you could take a few minutes to not just complete the survey but if possible to provide feedback. We use the surveys as a valuable tool in planning future webinars and improving webinars and then potentially other topics that you would like to have training on or have as a part of the webinar series. So, we'd really appreciate it if you could take to time to complete that brief survey immediately following this webinar.

Now, on to our presentation. Today's topic is the type of topic that it's not an easy topic to understand. So, if you have participated in this webinar before, you can never hear this information too much. It's the kind of information that unless you're actually involved in indirect rates, or computing them, or understanding them, it is a topic that the more you

hear it, the more repetitions you get, the better you start to understand the concepts.

If this is your first time participating, welcome. Don't feel overwhelmed if you don't grasp all the materials with this first training. If you're returning, hopefully there'll be some additional insight that will further your understanding of this particular topic.

I am Robin Booth. I am presenting this webinar. I'm the audit principle for Booth Management Consulting. Our firm is the contractor providing the quality audits technical assistance. We assist with action plans, with financial analysis, and trainings, and webinars, and performing the financial administrative reviews. A lot of you may have had contact or interactions, if not with myself, then with other members of our team.

Today, this is an effort to give you an understanding of indirect cost and indirect cost rates and just hopefully to give you that general, basic, foundational knowledge that as issues arise concerning this topic, you're at least familiar with what is in fact an indirect cost and indirect rate. What's the difference between direct and indirect costs? What's an unallowable and excluded cost? What does that mean?

How do I determine which indirect cost, if any that I want to charge on my budget under this particular grant? Do I want to do 10% de minimis rate? Do I have a negotiated indirect cost rate agreement? Maybe as a state agency, I want to do a cost allocation plan.

Then, we're actually going to go over some examples of computing the indirect cost rate for each of the various options that you have. For parents and intermediaries, we are going to address some of the things you need to be aware of as it relates to sub-recipients. Of course, we want to go over the overall retention requirements because no matter which rate or indirect cost rate you opt to use, you do have to retain certain records that if you're subject to audit, you're able to justify certain costs.

Then finally, we want to talk about how OHC can assist you within this particular area from computing your rates, to assisting you with budgeting and understanding your rates, to if you're a parent or agency to reviewing sub-recipient rates and other areas directly or indirectly associated with this topic.

Indirect rate, what is it? It's really a ratio or percentage that you're allocating the cost for you to be in operation and for you to have facilities, to actually be in a position to administer this particular grant. What the government recognizes is while there are direct costs associated with you performing the grant that are consistent with you achieving the purpose for the grant, you also have to be in operation. There are certain costs that are not direct, but they're associated with general and administrative expenses, with having a facility, and running a facility.

The government recognizes that and are amenable to paying their fair share of those costs, not 100% because they recognize that you're getting other grants and funding sources that you're also using these same costs to help administer. So they're not direct, and they don't want to be responsible or have the government unduly or unfairly burdened for costs that are not theirs. To the extent that a certain percentage of your cost to be in operation and have facilities are indirectly associated with that grant, they want to pay their fair share.

That's what that percentage or ratio is. It's just the government coming up with its fair share of those costs that are not directly associated with the grant but you have to incur to stay in business. Prior to, at least with the

Comprehensive Housing Counseling Grant, due to the dollar amount, if you didn't have a negotiated indirect cost rate agreement, you could not charge indirect costs.

For a lot of you, if you've had the Housing Counseling Grant historically, this may be a new cost line item on your budget because you weren't eligible for it before the uniform guidance which, as you all know, modified, or updated the whole OMB circular [ph]. So, now under that guidance, you have an option that you didn't have before. A lot of you may never have computed indirect costs or even were concerned with indirect rates. We're hoping that this will assist you in getting the understanding that you need to make the determination of whether you should be charging indirect costs as part of your Comprehensive Housing Counseling Grant.

So, how does it work? You provide services which the government would otherwise provide. That's the direct expenses. They're the direct counseling expenses. They're other direct costs directly associated with you performing those services that you've included in your work plan and meeting those goals.

These are direct expenses. Then, you incur some other expenses that you need to operate but they're not directly associated with the grant, but they're critical to your ability to perform the grant because if you're not in operation, you're not in a position to actually provide the services under the grant. The government says, we'll pay 100% of the direct expenses, but we're only going to pay our fair share of those other indirect costs.

To determine what our fair share is, we're going to use this ratio or percentage. That's what's called that indirect cost rate. That fair share or that rate that we use, you have three options for how you're going to determine what that rate is and then how you're going to multiply that rate times certain costs to say, okay these are my direct expenses. I'm multiplying this indirect rate against those expenses and then that's going to represent my indirect cost.

All of this we will go over in examples to further illustrate how the indirect cost rate works. It's important to understand that you have three real large options with a lot of sub-options under them if you choose to go in different routes. You can either, one, elect the 10% de minimis rate, and that becomes the rate that you use to compute your indirect costs, two, the negotiated indirect cost rate, or three, the cost allocation plan.

Now, we're going to go over each of these options. For you, as an agency, if you've never considered indirect costs before, these are your three options. The goal is to help you identify which option is best for your agency.

You should be doing the following steps to charge indirect costs to a grant. Understand that once you get this rate, you then have to do certain things from an accounting perspective to make sure you're multiplying that rate times what's called the base which is the right dollar amount to come up with what your indirect costs are. Step one is you have to segregate your direct costs for every grant, for every funding source from your indirect costs because remember the government wants to pay its share of the indirect costs, so those indirect costs should not be costs that are really associated with another grant or funding source.

If it's a direct cost to another funding source, then it shouldn't be in the indirect cost pool because somebody else is already paying 100% of that cost. The government wants to make sure your accounting system is designed, or your financial management system is designed to segregate the direct cost from the indirect cost because they don't want to pay any

share of somebody else's direct cost for what you're being 100% reimbursed.

Once you make sure your accounting system is doing those things, then you'll group all of your indirect costs for your organization. That's going to be indirect salaries for administrative people, or if you have a receptionist, or HR, or accounting, it'll be your offices, your utilities, your office expense, those things. Those costs will be grouped together because these are shared costs that every one of your grants absorb some part of in order for you to perform that grant.

Then, we have to decide what rate are we going to use? What indirect cost rate best meets my organization or do we qualify for? Once we determine what that rate will be, it determines the next step on how we actually compute the indirect cost.

As you can see, the first thing though is to make sure you clearly identify direct cost for each of the grants or funding sources. It doesn't matter if the funding source is not a federal award. If you have another grant from another organization and there are specifically direct costs, like you maybe have people on payroll or salaries that are providing the direct

services for that grant, then it's critical that those costs for that labor be bumped up against that grant as direct costs and not be included in your indirect cost pool. This is a cheat sheet on what you need to think about when you start to determine and compute your indirect costs.

I've talked a lot about direct versus indirect costs, so it's important that you understand what the difference is. Examples of direct costs, so we tried to pull out the examples that's associated with this grant. These are costs that are directly reimbursed from the grant. They pay 100% of these costs. They're in your budgetary line items. They're approved costs in your budget that are reimbursed at 100%. You have direct salaries and fringe benefits which are the two most common costs.

Then, other examples are travel, training, supplies, consultants, and sub-awards. Now, the critical issue is, if in fact you're being reimbursed for them, you have to maintain supporting documentation that, if subject to audit, clearly verifies that you've incurred these costs for this particular grant and that they are direct to that grant. The major difference, and this is the note here on the slide, between your direct and indirect is that only direct costs can be traced to a specific program or project.

I always say if you have budgets for any of your funding sources, and in that budget you've listed out what those costs or expenses are that you're being reimbursed for or that are included in the budget, they're automatically your direct expenses. It's not unfathomable that you might have one grant that allows you to have program expenses as a direct cost but in another grant, they don't cover that, so it's included in your indirect cost pool.

That is where your financial management system or accounting system becomes critical because you should be able to charge costs to each of the various grant or funding sources. For that funding source where the program expense was a part of the budgetary line item and it was approved as a direct cost, every time you're incurring those costs, you should be able to charge it to that grant separately as a direct cost in your accounting system.

Contrary if it's for your OAC where program expenses are not an allowable direct cost but you do incur some program expenses, you would have to include it in your indirect cost. That means that you would not be charging it to Office of Housing Counseling and it would be included in that pool of indirect costs. You can see how one type of cost can be

treated differently depending on the funding source and the requirements for that funding source.

That is why your financial management or accounting system becomes critical in how you're allocating costs as either direct or indirect and to the various grants and funding sources. Once again, direct costs, I'll say it over until you get it, they're specific. They're identifiable to that grant or funding source, and you would not otherwise incur them unless you had that funding source.

I always say if a cost disappears if you don't have that funding source, then that cost was direct to that funding source. Whereas indirect costs, they actually benefit multiple grants. They're not identifiable to any specific grant and/or service or activity, and they benefit, as I said, pretty much the entire organization.

In this indirect cost, there's 2CFR, the uniform guidance, sites two categories, facilities and administration. Just so you'll see I had a note there again, it is very important that you segregate direct and indirect costs in your accounting system, critically important. We're actually seeing, I say we as a company, we're seeing an uptick in federal agencies really

reviewing the financial management system for grant award recipients because they recognize how critical it is that your costs are being properly segregated from direct, to indirect, and even unallowable, and that they're being charged to the grant because if you're including those costs that are direct in your indirects, and you're charging indirect costs to the government, you're getting duplicate payment, maybe not 100%, on a cost that you've already received 100% payment for. So, there is greater emphasis on that.

The two broad categories, facilities and administration, facilities, think your building, think your utilities associated with that, if you have repairs and maintenance. All of those things are your facilities.

The administrative are just those general expenses that you incur. It may be dues and subscriptions. You might have various workshops and trainings that aren't specific to a grant. A lot of times it's administrative salaries like executive directors and all those things who may not work on a specific grant. Sometimes, it's program expenses. Sometimes, it's marketing. All of those expenses that you incur to be in existence to be able to go and continue to provide and perform on grants or other funding sources that do not fall within facilities are considered administrative.

This figure just illustrates for you what we mean. You have your indirect costs, administrative examples, and these are the types of services, or types of costs that are usually in that pool. Then facilities, these are the types of costs that are usually in that pool.

Just using this slide as an example will help you in making sure that when you set up your indirect costs and you have multiple pools, if you use both categories, administrative and facilities, you know where to put certain costs. One of the biggest areas that we always address is rent expense because just like I use as an example how a program expense could be charged as a direct cost and an indirect cost, rent is probably one cost that is mostly charged as direct and/or indirect. It has to be one or the other.

What happens is, a lot of agencies, because they've been able to really allocate rent as a direct expense, because they can show a methodology that clearly suggests that within our facilities cost, there's a certain square footage of space or area of space that we have to use just for your grant. For those individuals that are working that are providing housing counseling and you have to have certain meeting area or meeting space, and it's just for the HUD Housing Counseling Grant. Well, in that area

where you can justify that these costs, that rent, is specific to the Housing Counseling Grant, and you have a methodology that supports that it's specific to, and the most common methodology for rent is being able to clearly identify certain space that's just for housing counseling and identify the square footage of that space dividing it by the total square footage of that facility to get that percentage. That percentage is the percent that then can be charged as direct expense to that grant for rent and all of the associated utilities.

The thing about direct and indirect cost, there's no such thing as this cost is always direct or this cost is always indirect. The biggest thing you have to do is to be able to understand what justifies or what methodology supports your treatment of that cost. If you want to treat rent as direct cost, understand you have to have a methodology, which I've just summarized, that clearly supports that rent is in fact a direct cost. Otherwise, it gets treated as an indirect cost.

These are common direct and indirect costs. These are not end-all. There is flexibility depending on the types of awards. Sometimes we get a question that'll say, well, on another federal grant, they allow me to

charge this as direct. That could very well be true, and that is very well acceptable.

In this particular grant, these are the key or reoccurring and normal common direct costs. Then, commonly rent is treated as indirect cost unless you're able to provide sufficient justification. Then, we treat it as a direct cost.

Once again, this is yet another cheat sheet for you to look at your cost element and if you're just going through this process for the first time of segregating direct and indirect costs, you can use this to help determine which pool of indirect costs the various expenses to fall into. Then, once we've segregated so allocated to either direct or indirect, you still have to deal with the issue of if a cost is allowable or unallowable. The term unallowable is a cost that's specific to federal government grants and contracts.

It doesn't mean that it's not a valid expense. If it were in a contract, it would be tax deductible but for the federal government, there's just certain costs that they will not reimburse you for. It has to meet certain cost

principles which we have summarized here allowable, reasonable and allocable.

These cost principles are documented and stated specifically in the uniform guidance in sub-part E. Here we give you the reference to sub-part E and allowability being one of the first tests. To be allowable, you have to have in place a sufficient financial management system.

Everything that I just said, if you don't have an accounting system, it could be suggested that your costs aren't allowable because they can't verify your proper treatment of that cost in your financial management system or accounting system. You can read about that, as I said in 2CFR, part 200, sub-part E.

It has to meet the terms and conditions of the specific award, and yes, awards can have different terms and conditions. It has to ensure how to properly and efficiently administer federal funds based on its unique resources and experience. It has to meet that test. You have to be properly and efficiently administrating that and it cannot be in that category of expressly unallowable costs under 2CFR part 200 which we're going to go into.

To be allowable also it must be reasonable and necessary, and you can see that in section 200.403. These are all sections of the uniform guidance. It has to conform to limitations, consistent with your policies. You have to treat it consistently. Your costs can't be direct one day and indirect the next day or on the next grant unless you can justify. Remember, anytime you're deviating from a normal practice, you want to be able to justify.

It has to be consistent with general accepted accounting principles. It still has to meet those principles which has to deal more with valuation, and existence, and things like that which is why an accountant is important because they understand what's allowable or what meets those particular GAAPS, which is general accepted accounting principle standards, and it has to be adequately documented.

As we said, we give you all of the reference straight from the 2CFR. You now have to make that determination. You should be making it every time on both direct and indirect cost. Wherever that cost falls, if it doesn't meet this test for allowability, then it should be segregated into a group of accounts that are called unallowable which should also be in your financial management system.

It's just critical for you to understand it has to meet allowable requirements per the CFR. Under the CFR, you should take the time, especially your accountant or financial or whoever's involved in how you're charging or expensing your costs to the various grants, especially a federal grant. These are federal grant requirements.

These costs are expressly unallowable. When I say expressly unallowable, meaning unless somewhere in that federal grant agreement it makes them allowable, no matter what, they're unallowable, things like most of us know, alcoholic beverages, there are certain advertising and public relation costs that are unallowable. You need to read that section because everything that's advertising and public relations, a lot of it may be unallowable.

Contributions and donations, entertainment costs, fines, penalties, damages, and other settlements, these are the types of costs that if you're audited or even if you're trying to negotiate an indirect cost rate agreement for your agency, well, you would have had to establish within your accounting system accounts that are grouped together that are expressly unallowable. It's almost like having your own set of accounts that say,

well if it's a fines and penalty, this will be our chartered account number we'll charge it to. That'll go into a pool or a group of unallowable costs so we can make sure that when we compute our indirect costs we haven't included any of these costs either as direct costs or indirect costs.

You understand that we had to first determine that we group them together and segregate the direct versus indirect. Then, we had to determine if they were allowable and reasonable and necessary. We had to make those determinations.

Now, we can talk about our options for charging indirect costs. As we said earlier in the presentation, you have three key overarching options. You can opt for the 10% de minimis rate. You can negotiate an indirect cost rate agreement with the federal cognizant agency. You can prepare a very comprehensive cost allocation plan which is generally for state and local agencies and require a very in-depth and detail-oriented accounting system in order to justify.

With the 10% de minimis rate, well with each of them, we try to tell you how it's computed, and we tell you generally who uses which rate. That 10% de minimis rate, that's computed based on modified total direct cost.

We're going to go over modified total direct cost in slides immediately following this.

Most of the time, for those LACAs and small intermediaries that meet the requirements, because there are specific eligibility requirements for the 10% de minimis rate which we'll also go over in a series of slides following this one, if you meet those requirements, a lot opt for the 10% de minimis rate for various reasons. Now, the negotiated indirect cost rate agreement is a negotiated rate with a federal cognizant agency. For federal grants, you would have to negotiate this rate with the agency that awarded you your largest grant.

With every agency, there's a unit or a group, or division, or department that actually reviews submissions because you have to submit and incur a rate submission, and then they have to review that rate submission. They're going to look at all your expenses. You're going to give them a lot of information to verify that you've segregated the costs correctly direct and indirect, that the costs are allowable, they're reasonable and necessary, and that you've allocated them to the right contract so they're not in your pool. Then, we're going to negotiate what that rate should be based on the computations.

Generally, this is used by intermediaries and MSOs because it's a lot more complicated. It requires a lot more accounting and finance and time to negotiate. Out of all of these, that cost allocation plan is probably the most complicated because in this plan, you're taking every expense that you have and you're coming up with some kind of methodology so that you can charge it directly to each grant.

Pretty much, you're saying, every dollar we spend, we're going to figure out how we can charge it directly to each grant. With rent, okay, that's going to be based on square footage. With HR and maybe accounting, it's going to be based on hours worked.

So, every time an accountant does something, he's going to charge it to a grant, and we're going to look at his hours that he's charged per grant and his salaries, and we're going to figure out how much of that should be allocated to each grant. That's how complicated a cost allocation plan is. That's why it's usually used by state housing finance authorities and multi-state because one, they're required to do cost allocation plans.

Some pros and cons for the 10% de minimis rate. Eligible participants and sub-participants, now you're able to charge indirect costs because you don't have to have a negotiated rate. You don't have to get permission.

If you meet the eligibility requirements for that 10%, you can charge it now. It's giving you indirect cost rate to charge. You don't have to do any kind of submissions of indirect cost proposal or any kind of cost proposals for somebody to review. You're immediately eligible. It's no time delays or waiting for approval or acceptance. Once you make that determination if you meet the eligibility requirement, you can then elect that rate.

There's no negotiation, very easy to compute which we'll show you in our computation. You really don't have to have an in-depth knowledge of cost accounting or grant accounting. If you have general accounting knowledge and your system is generally set up, you should be okay with this one.

The biggest con is that you have to meet the eligibility requirements which we'll discuss momentarily. You're limited to 10%, so let's say that you figure out what your actual indirect costs are, and you do the ratio, and it's

really more than 10%. If you elect the 10%, that's the maximum you can use, and you have to continue to use that 10% unless or until you negotiate an indirect cost rate or some kind of cost allocation plan.

You can use a lower rate, but the maximum you can use is 10% using the 10% de minimis rate. Certain eligible activity components are unallowable, so when we look at the modified total direct cost, which is what MTDC stands for, you'll see that certain costs you will not be able to multiply that 10% by because it does not fall within the allowable and eligible activity cost for the 10% de minimis rate.

Then, you still have to track though. You have to track your salaries, your wages, still have to have a financial management system that's segregating your direct costs, and your indirect costs, but you don't have to have in your indirect costs, a separation of your facilities versus G&A expenses. They can all be grouped together, but you still have to track costs so you still need a financial management system.

For the negotiated indirect cost rate agreement pros, you usually can charge more than 10%. You're actually recovering. Your percentage is your actual indirect cost rate. Generally, you recover more because it's

based on your actual indirect cost rate. All federal agencies, they have to accept a negotiated rate. They can't tell you, you can't use it or you have to use the lower rate. They have to accept it.

And if, in fact, your organization grows and your indirect costs increase, you can go back and ask for approval or to renegotiate to get an increase in the rate. Under that scenario, the reality is you have a better opportunity to have a higher indirect rate to be reimbursed for.

Now, the cons as you can see just by looking at the number of cons versus pros, for this particular grant the cons are you have to submit and prepare indirect cost plans which is going to require experienced and knowledgeable staff to prepare. If you have to do any kind of indirect cost plan or submission, you're going to have to have accountants that really understand the cost principles and how to do the indirect cost rate. They're going to have to be able to negotiate.

You're going to have to pull supporting documentation for certain costs because they're going to ask about costs to see, wait a minute. Should that have been allowable or unallowable? Should that have been a direct or indirect? So, it's going to require more accounting systems to accumulate.

You're going to have to renegotiate this rate every three years. It's usually these rate negotiations, it can take an extended period of time. First of all you have to get your federal agency that awarded you the largest grant, they're whom will be your federal cognizant agency. You have to get them to agree to review your incurred cost plan.

Then, because of the backlog, it usually takes a lot of time. During that time period, you cannot charge any indirect costs while they're negotiating. Then, remember that it has to be renegotiated every three years, so every three years you have to submit all this documentation and information all over again.

It's great to the extent that you're an organization that has substantial or material indirect costs. If you're not, and your indirect costs are nominal, you're better off going with that 10% de minimis rate which is why that's usually what the smaller LHCAs do.

This cost allocation plan, well this assures that you get reimbursed 100% for every dime you spend, pretty much. That's what it does by grant or program because you're charging every cost you spend to a particular

grant. You're actually getting reimbursed or recognized for all of your actual costs. That's why state, local, and Indian Tribes over $35 million, they have to do it. They have to do a cost allocation plan. If I told you the indirect cost plan was complicated, this one is even more so, very complex.

You have to have extremely knowledgeable individuals on cost plans and cost policies. Your accounting system has to be very robust because you're using a lot of different units and tools to be able to track these methodologies. It's extremely time consuming. A cost allocation plan usually requires sometimes several full-time grant-costing or costing kind of professional that can help not just prepare but then monitor the costs as they come in to make sure they're being properly charged to each of the grants. It's very complex, very time consuming.

As we said, option one is for small recipients. You might want to consider this de minimis rate. Now, I kept mentioning the criteria. The criteria for selecting de minimis rate, and this is straight from the uniform guidance. It's not subjective. You have to meet this criteria. A lot of you may recall in your grant execution packages if you were electing the 10% de minimis rate, you had to certify that you met this criteria. That's saying that

you've never had a negotiated indirect cost rate agreement with any federal agency.

You have to use it indefinitely once elected unless and until you negotiate a rate. You have to determine what your base or what costs you're going to charge that rate against. You have to use a modified total direct cost as the basis. You have to meet all of these criteria. You can't meet two of the three or one of the three. You have to meet all of this criteria and this additional criteria.

If you receive over $35 million in direct funding, you cannot use this rate. You will be looking at state, local, and Indian Tribe cost proposals. You still have to maintain documentation supporting the methodology and the actual cost that you're including when you're computing the rate. I'll show you what that means when we get to the example.

You still have the same requirements of documentation and record retention, so that doesn't alleviate. It's not like you get 10% no matter what. No, you get 10% of costs that are allowable, reasonable, and necessary, so you still have to have that documentation.

Now, the modified total direct cost, which is the MTDC, that's the basis to which you multiply that 10% by. If you're electing this 10%, you have to use this particular base which we'll go over, but NICRAs and other agreements, you get to use different kinds of pools of cost to multiply it. That's why, if you're doing a 10%, you have to understand it's not subjective. You can only multiply 10% times these types of direct costs.

All Costs must be specifically identifiable to a grant or a funding source. Once again, your financial management system comes in to play. That has to be consistent with the federal award and your internal policies and procedures which all of us know that you have to have certain financial policies and procedures.

Now, in the modified total direct costs, there's certain direct costs that you can include when you're multiplying that 10% to get your indirect costs: all direct salaries and wages and the applicable fringe benefits, materials and supplies, services, and travel. Then, if you're an intermediary, you have sub-awards, sub-awards up to the first $25,000 of each sub-contract. That means that if you have ten sub-recipients, and all of them receive $25,000 or less, you can include the entire $250,000 or whatever it is as sub-awards, but if some of them receive more than $25,000, for each sub-

award, you can only include $25,000. We'll show you that in the computation.

You still have to meet the same cost principle though. It has to be identifiable to a particular funding source, and it has to still be reasonable and necessary and meet those principles for allowability. What you cannot include in the MTDC: equipment which is defined for these purposes and under uniform guidance and as an item of property that has an acquisition cost of $5,000 or more and an expected value of more than one year. If it's $5,000 or more, and its value is more than one year, like if you bought a printer that cost $6,000 that you know you're going to use for ten years, you cannot include that when you're multiplying your 10%.

If you bought a smaller printer that was $1,000, maybe it's one you set in your office, understanding that if you charge that printer to the grant, technically the federal government owns that printer, that printer may have a life of more than one year, so you still can't charge it. It has to meet both criteria to be included. That's why usually equipment is excluded because if it's not over $5,000, then the value is still more than one year.

Capital expenditures are also excluded: buildings, land, furnishings, alterations, renovations, telephone networks. Those things are also excluded from the modified total direct costs. Now, of course with a Housing Counseling Grant, for most of you, these aren't even a factor. They're not elements of your budget, so you don't have to worry about them.

We do get questions about some office equipment and things like that where we have to advise, based on what the uniform guidance says is allowable when computing the 10% de minimis rate. Other costs to exclude: rental costs, rental costs cannot be included, scholarships, and fellowships, participant support costs, notice I said rental costs, not rent costs. Now because if in fact you have rent expense that you're including as a direct cost, you still cannot include that when you're computing your MTDC because it's a rental cost. Whether the rental is office space, or whether it's a rental of equipment, you still cannot include that cost. We'll go over that momentarily.

Just a brief illustration real quick just based on what's usually the cost of the budgetary line items of a Housing Counseling Grant, you can include your labor, your fringe [ph], you sub-awards up to $25,000, training

supplies. You can't include, these are reoccurring or common budgetary costs for the Housing Counseling Grant, are things like rent, utilities, equipment, capital expenditures, program, and G&A expenses. That whole broad G&A, you cannot include that. We've seen general and administrative expenses, whatever that is, but that can't be included.

Now, when we get into what costs are in the MTDC, these are purely definitions right out of the 2CFR, your direct salaries and wages, your direct administrative, and clerical. To the extent you meet the requirements on the 2CFR for the administrative salaries, namely the justification, all of your fringe benefits, they can be included. For your fringe benefits, your [indiscernible] things like retirement, employer-paid taxes, health benefits, tuition, just your normal fringe benefits, those costs that are included in your rate, all of those can be included in the MTDC.

Your services contract, consultant fees they are allowable up to whatever contractual limitations they offer. For instance, in the Housing Counseling Grant, there's always a limitation on consultants or how much you can pay consultants annually and then by hourly rate. For last year's grant, it was $133,444 which is about $53.94 an hour.

It increased this year, so within your grant, to the extent that the limitations for consultants exceed that amount, you cannot include it. Travel costs, you can include travel costs, but remember you still have to maintain the right supporting documentation and you still have to meet the governing cost principles. Same thing with sub-awards and sub-contracts, up to the first $25,000; anything above that, you have to exclude.

In this example, we're going to go through this example. We're looking at a potential budget line item that was submitted by let's say an intermediary because we have sub-awards. So this intermediary, they have included in their budget direct costs, for salaries, you see fringe benefits, you see travel, and supplies, all of these things. This is what their budget says is direct costs, and that's fine.

They can charge all of these costs for their direct costs. Now, they're in the process of computing their indirect costs using the 10% de minimis rate. If you recall, under the 10% de minimis rate, they can only use a modified total direct cost.

When we go back to that same budget, and we say, okay, it's allowable for direct costs, but is all of it allowable for indirect costs for them to charge

that 10% by? When we look at each budgetary line item, and this is what you have to do, you have to say, okay, can I include this when I'm computing the indirect costs? Yes, because we know salaries are includable, so we're 100% of that.

Fringe benefits, they're eligible. We can include them in MTDC. Travel and supplies, they're fine. Equipment, no we can't include equipment. We talked about that. We have to exclude that.

The sub-awards, only up to the first $25,000. This one is $75,000, so we can only charge $25,000. This one is $20,000, so we can charge 100% of that one. This one is $25,000, so we can charge 100% of that one. So although the direct cost is $285,000, the eligible costs that we can use to compute the indirect costs is only $215,000. So, what that looks like, and this is the basis, this is what we've excluded. We excluded the equipment, the sub-contract in excess, and we've come up with now our MTDC. What do we do with this $215,000?

We then multiply that times 10% to get how much we can charge as indirect costs. We can only charge $21,500. The common error is that a lot of people not applying the principles of only using the modified total

direct cost will just take the total direct cost which was $285,000 and multiply that times 10% and then request or try to charge indirect costs at $28,500. Well, that is incorrect, and that's an improper payment and overcharging to the government. That is why you need to understand what's included in the modified total direct cost and what's not.

Another example, and this one we tried to give a little bit more complicated budget. These are our eligible costs. These are our ineligible costs. Then, once again, we go line item by line item, what's eligible?

We can include the salaries, 100% of the fringe, the travel. We have some equipment with a short-term life of less than one year. It did meet both things, so we included that equipment B, was greater than one year and we have examples down here, on the next page, the sub-awards we've computed and supplies.

Here, the equipment has a short-term life and is included in the MTDC and it's because it's not for one particular piece of equipment, it's multiple pieces of equipment which you should have said there with a short-term life. As opposed to this one piece of equipment they get that exceeds $5,000 and is greater than one year, we had to exclude that.

Then, we also had to exclude all of the awards over $25,000 to sub-recipients and then, the consultant fees that exceeded the annual amount limitation of this total direct cost in line 49 [ph], we had to exclude all of these items to get to the $715,444. This analysis slide that follows just explains what the assumptions were for how we excluded these items from the MTDC which is step one.

Here, we take this now, so this is our modified total direct cost. We multiply it by the 10%, and we get the correct amount, $71,544. The error would have been if we'd included all of the direct costs in that $949,000 and multiplied that times 10%, we would have gotten a direct cost of $94,000 which is a $20,000 some difference which can be material.

How does this look when I'm actually doing my budget and what are my challenges? Let's assume for the $949,000, the total grant award for this budget was $1 million, so we're charging all of the direct costs. Notice that none of the direct costs has been reduced because they didn't qualify for the modified total direct cost.

We just reduced them in computing the indirect costs. We're still charging 100% of the actual direct cost in our budget. What happened was, even though we computed an indirect cost of $71,544, we can only charge indirect costs up to the grant award amount.

Charging indirect costs cannot exceed what the grant award amount was. So, a lot of times, and you all have done it for the first time, you noticed that it became a plug [ph] number because you couldn't exceed the 10%. We know that 10% for this budget was $71,544, but because the total award amount was $1 million, we couldn't charge more than what would have taken it to the award amount.

That's what a lot of you will see when you're doing your budget. The issue is, you still have to compute it though to make sure that you're not charging more than what is the actual indirect cost. That's the computation we do as a part of the grant execution process, so a lot of you will not get a dollar-dollar match for that, but what you cannot do is you cannot charge more. You cannot try to increase your award in order to charge all of what you computed as your indirect cost.

The next example, the negotiated indirect cost rate agreement, which as I said, this is negotiated and in your actual agreement it tells you what kinds of rates that you had and what rates you have. In a NICRA, there's different rates that can be there. It can be a provisional rate which is a temporary rate that they giving you to a grant period.

Sometimes they give you these rates because they haven't finished their review of your agreement or because you may be new and you don't have the history. So, they're giving you're a temporary rate so you can still bill and charge some type of indirect costs until they get you your final rate which is the actual rate that's determined at the end of your base period. Even though every three years, you renegotiate your rate, every year you have to compute your final rate and use that rate.

A predetermined rate is a rate that's already established in certain grant agreements or certain funding sources will say no matter what, you can only use this rate. I don't care what you're negotiated rate is, this is a predetermined. That's the only rate that you can use.

Then, you may be able to do a fixed rate carry forward for larger grants which basically says that we're going to use this rate for two years.

Instead of annually reevaluating, we're going to do it over two years, and then annually thereafter. Once again, this is really to help especially when there's a backlog so that you can build these indirect costs because if you have a negotiated indirect cost rate agreement, you have to have some rate that you can bill against.

Those are the types of indirect rates that will be included in your indirect rate agreement. This is just an example of an indirect cost rate negotiated agreement. Here you can clearly see it tells you what kind of rates you have, what's the effective period, what rates you can use, what programs you can apply it to. It also tells you what your base is.

If you remember with the 10% de minimis rate, the base is always the modified total direct cost. There was certain expenses that you could not multiply that rate by. Same thing here, that means when this agency computes their rate, they can only multiply this 14.9% times total direct cost, less capital expenses and pass-through funds.

They have to exclude capital expenditures and pass-through funds. Pass-through funds would be our sub-awards. Notice though, their pass-

through funds don't have that limitation of up to $25,000 so where they can include some of it. This is saying all pass-through funds.

That's why when you get a rate agreement, you clearly have to read it and make sure you know how long the rate is effective, what base, how do you apply or multiply that rate times what cost and what programs it's applicable to. That's exactly what I said. That's all the things we just looked at on that particular rate agreement.

You want to review your NICRA. If you're new to the program, you want to check with accounting to make sure you know if they have a NICRA and if they do, you need to understand which rates you're going to use. Then, you want to make sure the rate is still effective because as you saw in the examples, there's an effective period.

So, if that period has expired, you need to get some kind of written understanding of where it is in the rate agreement. Now, if your rate agreement has expired, and you've already computed your new rate, while they're negotiating your new rates, we recommend that you err on the side of caution and use your lower rate, the lowest rate out of your existing rate that's the new rate you computed or the lower of your old rate.

Even when they come back and give you your rate, in a worst case, you'd have been using a low rate. You don't want to use the highest rate of the two. That's exactly what this slide talks about. You have to verify the base. I showed you on that agreement how it tells you what you can multiply these costs by. You have to verify that. Then, these are some of your common allocation bases, some of which we just saw.

Then, of course, number three is the one you have to use for the 10% de minimis rate. For those of you that have a NICRA, you're going to multiply the verified rate by the verified base. Then, you're going to compare the computed total to the budget, submit it to the agency, and you'll discuss any variances. Once again, your total direct and indirect costs cannot exceed award amount.

The same way for the indirect cost under the 10%, we had to fit a number in there, the same happens with your NICRA. Just because your actual computed indirect cost may be X, it cannot exceed the award amount. So, you'll either have to adjust your direct costs, or you'll just scale down to be within the parameters of your contract award.

For option three, the cost allocation plan, this is a very extensive document, the state, local, and government, and public assistance program. You can do several methods. The simplified method, you only have one single function. You're charging all costs to that particular function as opposed to multiple allocations. We have a lot of different programs with varying degrees of benefit and usually this is what the state and local government agencies have to use.

Then, you have the direct allocation which is all costs are charged directly to programs except for general and administrative. Indirect costs are pooled and allocated to indirect costs objectives. Some other things, and I didn't spend a lot of time purposely on cost allocation plans because that's really for the state and local agencies. If you have one, you have a team of knowledgeable professionals that are responsible for it. For you, you would just have to make sure you get a copy of it to include with your grant.

Other things you might want to know, for federal agencies, pass-through and sub-recipients, you can use a 10% NICRA. All of the pass-through clauses and conditions that are in the grant agreement they pass through to you. So you can use an indirect cost rate.

Your parent cannot tell you that you can't use indirect cost rate whether it be the 10%, or the NICRA, or the cost allocation. Understand that you can charge indirect costs. You are able to allocate and charge 100% of that cost directly. You may continue to do so.

If you can claim reimbursement for indirect costs, it's not mandatory, you don't have to now all of a sudden say, I have to include indirect cost. If you can use all your grant funds with direct costs, so be it. This is just now the government trying to provide you some subsidy or assistance with covering those other costs.

If the sub-recipient has a NICRA, they must use the NICRA; however, a sub-recipient cannot use a parent's NICRA. Just because a parent has negotiated a rate, their sub-recipients cannot use their negotiated rate. They would have to make the determination of which one of the options that they have.

It's not permissible for pass-throughs to force or entice a proposed sub-recipient without a negotiated rate to accept less than the 10% de minimis rate. If, in fact, their budget within their award amount they can request a

total 10%, then they should. The parent should not in any way suggest, well you know a change your direct costs or we don't really want you to include all of that in direct costs. If it's within that 10%, and it's computed correctly, then you can charge those costs to the grant.

Retention of records, as you can see, you can clearly understand why you still have to maintain records because you're still charging everything to your costs. So, you still have to be able to verify and justify those costs that you're multiplying whatever that rate against whether it's salaries, fringe benefits, whatever it is. The retention of records stays the same. You can refer to the section 200333 for that.

How OHC can assist you, some of the technical assistance in this area has to deal with your policies and procedures across policies and procedures, helping you do your indirect cost application and calculation, reviewing your schedule of indirect cost, looking at your timesheets and your quarterly reporting because timesheets become the critical supporting documentation.

From financial analysis, we can do a financial capability assessment which would include looking at your indirect cost rate, review of your sub-

grantees, if you wanted to review their 10% modified indirect cost rate computations or indirect cost rate. The accounting system review is big because we can actually help you look at your financial management system and assist you in configuring it so you're properly allocating costs to direct and indirect and you're maintaining that system consistent with the uniform guidance. That's a big area we're doing more and more on, from configuring your accounting system to training staff on how to properly review costs and make sure you're making the decision whether it's direct or indirect, allowable or unallowable, if it should be charged to a grant or if it should be charged to one of the indirect cost pools.

I just talked about the training that we do about that. We can do a readiness assessment too especially on your accounting system to do an assessment of if your accounting system is in compliance. Then the recommendation may be, if we determine your accounting system is compliant, then great. If not, then we may recommend technical assistance or training or whatever is needed for you to get your financial management system in place.

The process for this stays the same. If you haven't heard it before, you have to request assistance from you HUD POC. If in fact, you're a sub-recipient, you should request assistance through your parent.

Then, they will request it through the POC or you can request it from the HUD POC if you him directly, but you must include any such requests through your parent organization unless they tell you otherwise. If they say they want you to make any requests directly through the parent and then to HUD, that would be between you and the parent.

The POC would then have to approve the services and then they would initiate the assistance. So, once it's approved, then usually it's a one to two business day turnaround. That's at the most from the time that the request is made to the approval and then we start initiating services.

As I said, this is a lot of material, so we used every minute of this entire hour webinar for this. If you have any additional questions, you can send them to housing.counseling@hud.gov. If you put Understanding Indirect Cost Rates or any version of this in the subject line item, we can make sure it gets to the appropriate person for a response.

Thank you for your time this afternoon, and have a nice day.

Moderator Ladies and gentlemen, that does conclude our conference for today.

Thank you for your participation. You may now disconnect.