

# Texas Workforce Commission

## Adult Education and Literacy



## Summer Business Meeting 2020

### Handout

July 29, 2020

Day 1, Session 2

# Cost Principles

Presenter: Jenny Noren, TWC Financial Initiatives

This session will describe the role that cost principles play in grant management, identify where to find the cost principles that apply to TWC grant awards, review selected cost-related topics (including general allowability factors) and reiterate the U.S. Department of Education restrictions on indirect cost rates.

## Contents

<b>Objectives .....</b>	<b>4</b>
<b>Cost Principles: The Role They Play in Grant Management &amp; Where to Find Them.....</b>	<b>4</b>
Grant Programs.....	4
Grant Requirements.....	5
Allowable or Unallowable?.....	5
Cost Principles & Grant Requirements.....	5
Policy Guide (2 C.F.R. § 200.400).....	6
Cost Principles: Breakdown.....	7
Selected Cost Related Topics.....	8
<b>Direct Costs versus Indirect Costs .....</b>	<b>9</b>
Total Cost of a Grant Award: Allowable Direct Costs + Allocable Indirect Costs – Applicable Credits.....	9
Direct & Indirect Costs .....	9
Indirect Costs: Two Broad Categories .....	10
Facilities.....	11
Administration.....	11
Allocation: Cost Allocation Plan versus Indirect Cost Rate.....	11
Special: Restricted Indirect Cost Rate.....	12
<b>Factors Affecting Allowability of Costs .....</b>	<b>12</b>
Be Necessary .....	12
Be Reasonable .....	13
Be Allocable.....	13

Conform to Limitations/Exclusions .....	14
Be Consistent .....	14
Be Determined in Accordance with GAAP .....	14
Not Be Included in Cost Sharing or Matching .....	14
Be Adequately Documented .....	15
What is Adequate Documentation?.....	15
Some Documentation Practices .....	15
<b>Considerations Relating to General Provisions for Selected Items of Cost .....</b>	<b>16</b>
Selected Items of Cost .....	16
Prior Approval .....	17
<b>Unallowable Costs .....</b>	<b>17</b>
Responsibility for Unallowable Costs.....	17
Some Allowable Cost Findings .....	18
Some Practices to Help Avoid Unallowable Costs .....	18
<b>Wrap-up .....</b>	<b>18</b>
<b>Questions .....</b>	<b>19</b>

## Objectives

This session will:

- Describe the role that the Cost Principles play in grant management.
- Identify where to find the Cost Principles that apply to TWC grant awards.
- Review selected cost related topics (including general allowability factors).
- Reiterate the U.S. Department of Education restrictions on indirect cost rates.

## Cost Principles: The Role They Play in Grant Management & Where to Find Them

### Grant Programs

- Taxpayers pay taxes.
- Tax revenues are public funds.
- Government makes laws to create public programs.
- Government finances public programs with public funds.
- Government administers public programs through grants.
- Grants identify laws, regulations, and other requirements.
- Grantees administer programs according to requirements.
- Government oversees compliance with requirements.

## Grant Requirements

- Laws
  - Relevant program legislation
  - Other relevant laws
- Regulations and Rules
  - Program regulations
  - Federal awarding agency regulations
  - OMB “Uniform Guidance” (UG) (2 C.F.R. Part 200)
  - Texas “Uniform Grant Management Standards” (UGMS)
  - TWC Rules
- Terms and Conditions of the Grant Award

## Allowable or Unallowable?

**Allowable:** Meets grant requirements.

**Unallowable:** Does not meet grant requirements.

## Cost Principles & Grant Requirements

Cost Principles are only one part of the grant requirements. The Cost Principles are part of the UG and UGMS. (The UG and UGMS also contain administrative and audit requirements.)

Grants also include other requirements. To be allowable a cost must comply with the Cost Principles as well as all other grant requirements.

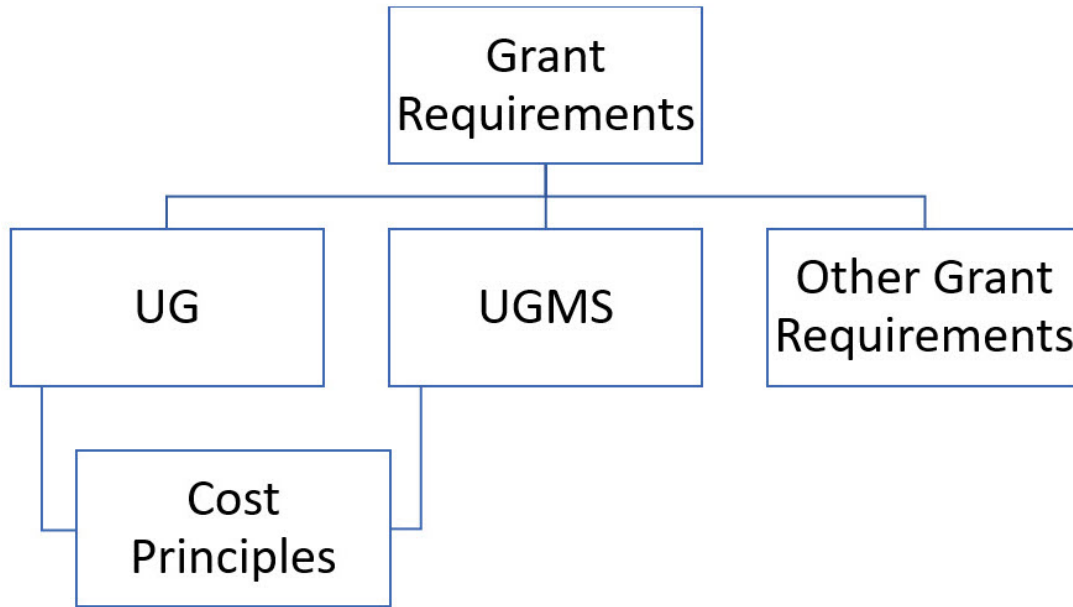


Figure 1: Hierarchy shown grant requirements

Policy Guide (2 C.F.R. § 200.400)

Fundamental premises on which the Cost Principles are based:

- Grantee is responsible for efficient and effective grant administration through the application of sound business practices.
- Grantee assumes responsibility for administering grant funds consistent with underlying agreements, program objectives, and the terms and conditions of the grant award.
- Grantee, in recognition of its own unique combination of staff, facilities and experience, has the primary responsibility to employ whatever form of sound organization and management techniques may be necessary to assure proper and efficient grant administration.
- Grantee’s accounting practices must:
  - Be consistent with the Cost Principles,
  - Support accumulation of costs as required by the Cost Principles, and

- Provide for adequate documentation to support costs charged to the grant award.
- In reviewing, negotiating and approving cost allocation plans and indirect costs, a grantee's cognizant agency for indirect costs should generally assure that the Cost Principles are applied on a consistent basis.
- Grantee generally may not earn or keep profit from the grant award.

## Cost Principles: Breakdown

**Basic Considerations:** composition of costs, factors affecting allowability of costs, reasonable costs, allocable costs, applicable credits, prior written approval, limitation on allowance of costs, special considerations, collection of unallowable costs, and adjustment of previously negotiated indirect (F&A) cost rates containing unallowable costs.

**Direct & Indirect Costs:** classification of costs, direct costs, indirect (F&A) costs (including cost allocation plans and indirect cost rates), required certifications, special considerations for State, local, and Indian tribal governments, and special considerations for institutions of higher education.

**General Provisions for Selected Items of Cost:** considerations for selected items of cost, and selected items of cost.

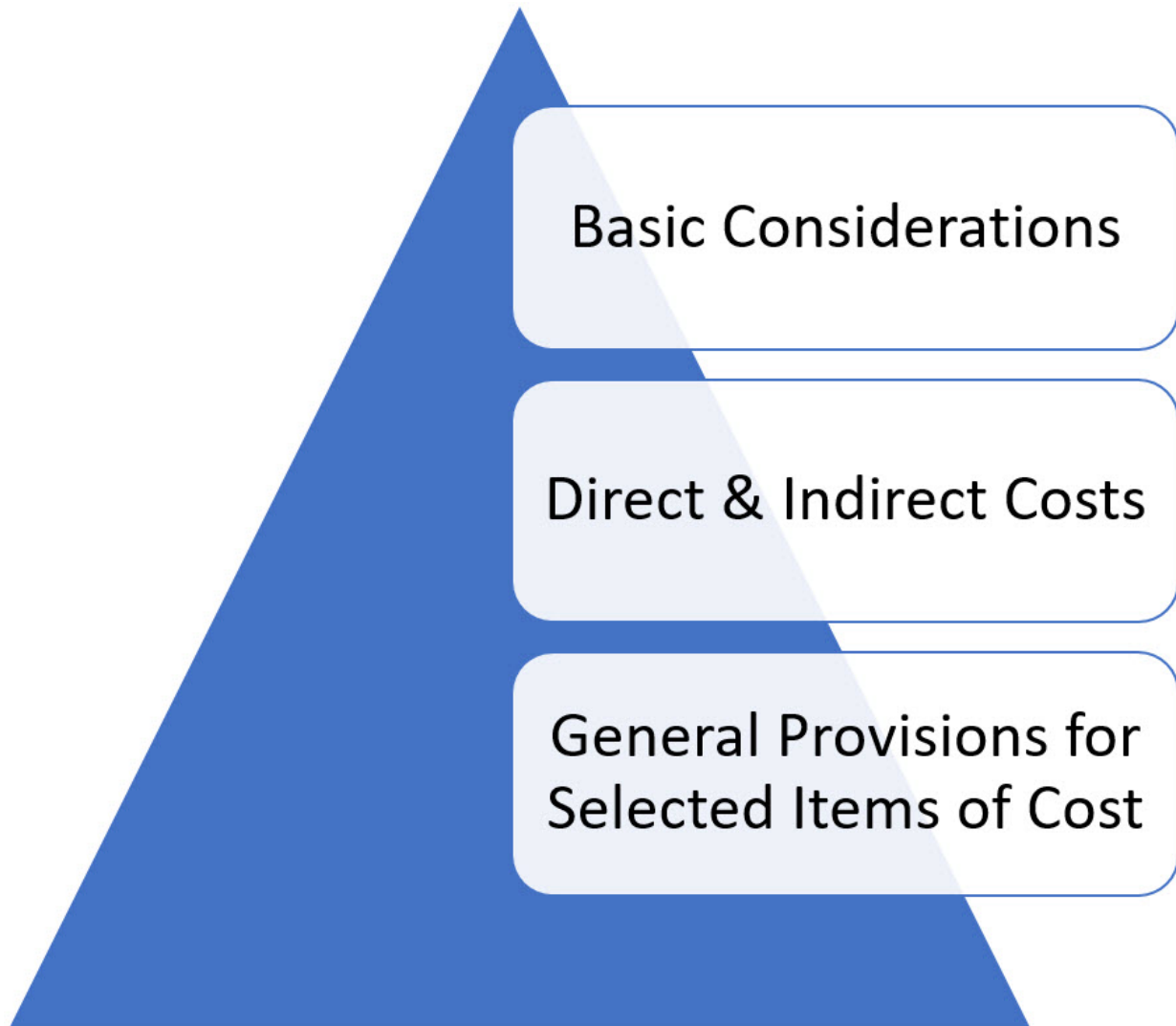


Figure 2: Cost Principles Breakdown

## Selected Cost Related Topics

This session covers the following cost related topics:

- Direct costs versus indirect costs
  - Special note on restricted indirect cost rates
- Factors affecting allowability of costs
- Considerations relating to the UG and UGMS "General Provisions for Selected Items of Cost"



- Examples of allowable cost findings

## **Direct Costs versus Indirect Costs**

Total Cost of a Grant Award: Allowable Direct Costs + Allocable Indirect Costs – Applicable Credits

The total cost of a grant award consists of the sum of allowable direct costs and allocable indirect costs, less applicable credits.

Applicable credits refer to receipts or reduction-of-expenditure-type transactions that offset or reduce costs.

- Purchase discounts
- Rebates or allowances
- Recoveries or indemnities on losses
- Insurance refunds or rebates
- Adjustments of overpayments or erroneous charges

Credit against allowable costs of the grant award(s) as a cost reduction or cash refund, as appropriate.

**Note:** Total Cost is not the same as Project Cost. Project Cost refers to total allowable costs of the grant award + cost sharing. Cost sharing refers to required cost sharing and voluntary committed cost sharing, including cost sharing from third party in-kind contributions.

## **Direct & Indirect Costs**

Each cost is classified as either a direct cost or an indirect cost.

## Direct Cost

- Can be identified specifically with a particular final cost objective or can be assigned to such activities relatively easily with a high degree of accuracy.
- Direct costs can be traced to final cost objectives in a cost-effective way.

## Indirect Cost

- Incurred for a common or joint purpose.
- Benefits multiple cost objectives.
- Not readily assignable to cost objectives specifically benefitted without effort disproportionate to the results received.
- Allocated to final cost objectives.

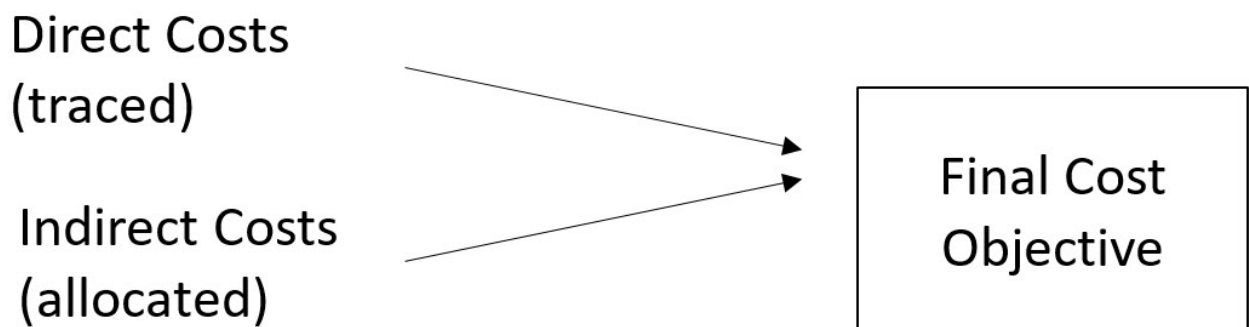


Figure 3: Direct Cost vs Indirect Costs

## Indirect Costs: Two Broad Categories

The Cost Principles require major Institutions of Higher Education (IHEs) and major non-profit organizations to classify indirect costs in two broad categories, "Facilities" and "Administration."

## Facilities

- Depreciation on buildings, equipment and capital improvements
- Interest on debt associated with certain buildings, equipment and capital improvements
- Operations and maintenance expenses
- Library expenses (major IHEs)

## Administration

General administration and general expenses such as:

- Director's office
- Accounting
- Library expenses (major non-profit organizations)
- Personnel and all other types of expenditures not listed specifically under one of the subcategories of "Facilities" (including cross allocations from other pools, where applicable)

## Allocation: Cost Allocation Plan versus Indirect Cost Rate

- Cost allocation plan
  - Usually multiple cost pools with an appropriate distribution base for each pool.
  - Program's percentage share of pooled costs changes each period according to that program's relative share of the distribution base for that period.
  - May be used to allocate organization-wide, central service, division or department costs, or shared costs.
- Indirect cost rate plan

- Applies the same rate(s) (percentage(s)) over the course of a specified period, usually the entity's fiscal year.
- Usually used to allocate organization-wide costs.
- Where an indirect cost rate is used with a Federal award or subaward (subgrant), that rate must be identified in the grant award.
- Each has its own unique cost principle requirements.

### Special: Restricted Indirect Cost Rate

- U.S. Department of Education: 34 C.F.R. §§ 76.563 – 76.569.
- Applies to TWC's AEL grant awards.
- Limits indirect costs to the product of the restricted indirect cost rate and total direct costs of the grant minus capital outlay, sub-grants, and other distorting or unallowable items, as specified in the grantee's indirect cost rate agreement.
- The restricted indirect cost rate equals the lesser of:
  - The restricted indirect cost rate in 34 C.F.R. § 76.564(a), or
  - An indirect cost rate of eight (8%) percent.
- Exceeding the limit and overallocation of indirect costs is unallowable.

## Factors Affecting Allowability of Costs

Except where otherwise authorized by statute, costs must meet the following general criteria

### Be Necessary

Costs must be necessary for performance of the grant award.

**Note:** Not further defined by the UG or UGMS. Considering Federal appropriation law:

- Does not necessarily mean “necessary” in the sense that the grantee cannot achieve the grant objectives without it.
- However, must be more than being desirable or important.
- A relative concept. There must be a logical relationship between the cost and the grant.
- Must not be provided for by some other source of funds.

## Be Reasonable

Costs must be reasonable for performance of the grant award.

- Per UG and UGMS, factors to consider include but aren’t limited to:
- Prudent under the circumstances prevailing at time of decision
- Ordinary and necessary, sound business practice, arms-length
- Market prices
- Requirements of applicable laws, regulations, etc.
- Responsibilities to employees, government, public
- Significant deviations from entity’s established practices which may unjustifiably increase the grant award’s cost

## Be Allocable

Costs must be allocable to the grant award—chargeable or assignable to a grant/cost objective in accordance with relative benefit received.

- Incurred specifically for the grant award;
- Benefits the grant award and other work, and can be distributed in proportions that may be approximated using reasonable methods; or

- Necessary to entity's overall operation and assignable in part to the grant award in accordance with the Cost Principles.

## Conform to Limitations/Exclusions

Costs must conform to any limitations or exclusions set forth in the Cost Principles or in the grant award as to types or amount of cost items.

Examples:

- Prohibitions on certain costs, practices, activities
- Limitations on administrative costs and indirect costs
- Caps on salaries, consultant fees, travel rates, etc.
- Costs that require prior approval

## Be Consistent

Costs must be consistent with policies and procedures that apply uniformly to both federally- and state-financed, and other activities of the entity.

## Be Determined in Accordance with GAAP

Costs must be determined in accordance with Generally Accepted Accounting Principles (GAAP) (except, for state and local governments and Indian tribes only, as otherwise provided for in UG).

## Not Be Included in Cost Sharing or Matching

Costs must not be included as a cost or used to meet cost sharing or matching requirements of any other federally-financed program in either the current or a prior period.

## Be Adequately Documented

Costs must be adequately documented.

Note: Recordkeeping is at the heart of grant oversight.

Only by requiring documentation that supports costs is TWC able to verify that funds were expended for authorized purposes.

Therefore, each grantee has a responsibility to maintain adequate records to support the allowability of costs claimed under a grant.

### What is Adequate Documentation?

- Documentation that demonstrates allowability.
- Examples:
  - Audit trail (step-by-step record by which a cost can be traced to its source)
    - Identifies the cost.
    - Shows when the cost occurred.
    - Shows approval by authorized personnel.
  - Additional information as needed.
    - Expanded description that includes purpose or use.
    - Circumstances in effect when decision was made to incur the cost.

### Some Documentation Practices

- Policies and procedures that define required documentation to support costs and all transactions.
- Do not use white-out on documentation.

- Make corrections in ink (not pencil).
- Sign/initial and date error corrections.
- Include written explanation for error corrections.
- Ensure documents are legible, including electronic record retention.
- If retaining records by scanning, controls aimed at preventing alteration
- Explain departures from established practices when the departure occurs.
- Use of prenumbered consecutive documents.

## **Considerations Relating to General Provisions for Selected Items of Cost**

### Selected Items of Cost

- The UG and UGMS include "General Provisions for Selected Items of Cost."
- In considering the allowability of a specific item of cost:
  - The "General Provisions for Selected Items of Cost" apply in addition to the UG and UGMS "Basic Considerations" for costs.
  - The "General Provisions for Selected Items of Cost" apply regardless of whether cost is direct or indirect.
  - Omission of a specific cost from the "General Provisions for Selected Items of Cost" does not imply that the cost is either allowable or unallowable.
  - For allowability of costs not listed, consider treatment for similar or related costs, and the UG and UGMS "Basic Considerations" for costs.



- In the event of discrepancy between the UG and UGMS “General Provisions for Selected Items of Cost” and the Federal award that TWC received, the Federal award will prevail.

## Prior Approval

Some costs require prior approval from TWC.

- Refer to the grant award, TWC Financial Manual for Grants and Contracts, UG and UGMS.
- Submit request to TWC Grant Manager.
- Use TWC Form 7100 if the request is for equipment.
- Do not complete purchase prior to receiving TWC concurrence or nonconcurrence.
- In some cases, TWC may be required or determine it prudent to obtain prior concurrence from the respective Federal awarding agency before responding to the grantee.

## Unallowable Costs

### Responsibility for Unallowable Costs

- TWC compliance monitoring.
- Where a cost is not allowable, the Government has a “reversionary interest” in the grant funds.
- TWC cannot relieve a grantee of the grantee’s liability for improper expenditures under a TWC grant award and has a responsibility to collect such debts from the grantee.

## Some Allowable Cost Findings

1. Inadequate justification for food/beverage costs.
2. Memorabilia purchases.
3. Clothing apparel for employees.
4. Outreach items having no connection to the program.
5. Purchases of décor for a meeting.
6. Travel without explanation of business need.
7. Merit increases without supporting documentation.
8. Services to ineligible participants or eligibility not documented.
9. Journal entries with no supporting detail.

## Some Practices to Help Avoid Unallowable Costs

1. Operationalize administrative and cost requirements.
2. Read and understand the grant requirements.
3. Maintain, review, and test policies and procedures.
4. Train and oversee staff.
5. Information flow/communication.
6. Scrutinize purchase requests and decisions.
7. Separately track unallowable costs.
8. Demand adequate documentation.

Hopefully, the information in this session will help you avoid unallowable costs.

## **Wrap-up**

That concludes this session. To recap, today we covered the role that the Cost Principles play in grant management and where to find the Cost

Principles that apply to TWC grant awards. We also reviewed selected cost related topics. Specifically, we reviewed the distinction between direct costs and indirect costs, and noted a U.S. Department of Education restriction for indirect cost rates. We also discussed general factors affecting the allowability of costs, and considerations to keep in mind when referencing the UG and UGMS “General Provisions for Selected Items of Cost.” We concluded, just now, with discussion about unallowable costs.

## **Questions**

If you have questions about this session, please e-mail TWC’s Fiscal-TA mailbox at [fiscal.ta@twc.state.tx.us](mailto:fiscal.ta@twc.state.tx.us).