Indirect Cost Allocation Plans

Introduction

The decision to recover indirect costs on state and federal grants should not be made lightly. For many small agencies, the cost of developing and maintaining an indirect cost rate is greater than the related benefits, particularly if the agency typically is able to expend all or nearly all of a state or federal grant through the reimbursement of direct costs only.

However, there are several reasons why an agency should consider developing a cost allocation plan and an indirect cost rate:

- Allows the agency to recover administrative costs.
- Enables the agency to determine the full cost of projects and services.
- Enables the agency to develop billing rates for services provided to non state and federal agencies.
- Allows the agency to manage funds more effectively by identifying all administrative/overhead costs, placing the agency in a position for possible additional funding if they are not capturing all of state or federal grant through the reimbursement of direct costs only.

Indirect Cost Allocation Plans

An indirect cost allocation plan is the documentation prepared by an agency to substantiate its request for the establishment of an indirect cost rate in accordance with the Title 2 Code of Federal Regulations Part 200.

Direct vs. Indirect Costs

Direct Costs are those costs that can be identified specifically with a particular final cost objective, such as a federal project or other internally or externally funded activity, and that can be directly assigned to such activities relatively easily with a high degree of accuracy.

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

Costs incurred for the same purpose in like circumstances must be treated consistently as either direct or indirect costs.

It is possible to justify the handling of almost any kind of cost as either direct or indirect. Labor costs, for example, can be indirect, as in the case of maintenance personnel and executive officers; or they can be direct, as in the case of project staff members. Similarly, materials such as miscellaneous supplies purchased in bulk – pencils, pens, paper – are typically handled as indirect costs, while material required for specific projects are charged as direct costs.

Costs usually charged as direct

- Project staff
- Project fringe benefits
- Consultants
- Project supplies
- Publications

Costs either charged as direct or indirect

- Telephone charges
- Computer use
- Project administrative personnel
- Postage and printing
- Miscellaneous office supplies

Costs usually charged as indirect

- Utilities
- Rent
- Audit and legal services
- Administrative staff
- Facility maintenance

Advantages of Indirect Cost Allocations

In addition to the direct cost of providing services, agencies also incur indirect costs. Such indirect costs include shared administrative expenses such as legal, finance, human resources, facilities, maintenance and technology. Certain important management objectives can be served by allocating these indirect costs such as measuring the cost of services, establishing fees and charges and requesting reimbursements under state and federal grants.

Through the establishment of an indirect cost rate, agencies are able to include indirect costs as reimbursable item on state and federally funded projects. Although the use of an indirect cost rate does not increase the value of the state or federal grant, it does provide an additional method for funding indirect costs and in some cases, improve cash flow.

However, establishing and maintaining an approved indirect cost rate is a time-consuming and complicated process. An agency that establishes an indirect cost rate is committing to a significant level of effort annually to develop the cost allocation plan and all the required supporting documentation. The decision to develop an indirect cost rate should be include the following considerations:

- Size of the agency
- Magnitude of indirect costs
- Expertise of financial staff
- Complexity of financial system
- Cost of developing and maintaining an indirect cost rate vs the benefits
- Percentage of state and federal funding to total budget.

For many small agencies, the cost of developing and maintaining an indirect cost rate is greater than the related benefits, particularly if the agency typically is able to expend all or nearly all of a state or federal grant through the reimbursement of direct costs only. For such agencies, continuing to bill only direct costs or using the De Minimis rate is preferred. Under Title 2 Code of Federal Regulations Part 200, agencies that have never received a negotiated indirect cost rate and receive less than $35 million in direct federal funding may elect to charge a De Minimis rate of 10% of modified total direct costs. Modified total direct cost means all salaries and wages, applicable fringe benefits, materials and supplies, services, travel and up to the first $25,000 of each subaward (regardless of the period of performance of the subawards under the award). Modified total direct cost excludes equipment, capital expenditures, rental costs and the portion of each subaward in excess of $25,000. A De Minimis rate may be used indefinitely. Costs must be consistently charged as either direct or indirect but may not be double charged or inconsistently charged as both.

Resources:
- CFR
- Caltrans Local Programs Procedure Manual
- Caltrans Audits and Investigations Indirect Cost Allocation Plan Submission Process