Practical Approaches to Cost Allocation

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Cost Allocation

- The **process** of assigning two or more programs the shared cost of an item or service.
Head Start Act Sec. 644(c): Policies and procedures shall be established to ensure that indirect costs attributable to the common or joint use of facilities and services by programs assisted under this subchapter and other programs shall be fairly allocated among the various programs which utilize such facilities and services.
The method developed by an organization receiving funding for more than one program, which enables the organization to fairly and equitably allocate the shared costs of the organization to each of its programs.

Hint: Existing regulations do not require a written cost allocation plan. However, grantees must be able to demonstrate that shared costs have been allocated fairly. To meet this standard, and financial management systems requirements, a written cost allocation plan is highly recommended.
The Importance of Accurate Cost Allocation

- Cost allocation is an integral part of effective fiscal management.
- Impacts planning, budgeting, reporting, internal controls and monitoring.
- Provides an accurate picture of how the organization spends all of its program dollars.
- Allows anticipation of the impact of funding changes (e.g. reduced state early childhood funds).
- Contributes to maximizing non-Federal share.
Keys to Cost Allocation

- Clearly define who, what, when, where and how the agency provides services – eligibility, enrollment, operating hours, location.
- Identify what costs are direct and what costs need to be allocated.
- Consider possible allocation methods based on actual agency operations.
- Select the allocations method(s) that best support the agency’s fiscal operations.
- Develop or update cost allocation plans annually and apply allocations monthly to monitor spending and compare to budget.
- Periodically review for currency and consistency.
Allocable Costs

A cost is allocable [can be charged] to a Federal award if treated consistently with other costs incurred for the same purpose under like circumstances and if it is:

- Incurred specifically for the award,
- benefits both the award and other program services and can be distributed in reasonable proportion to the benefits received, or
- is necessary to the overall operation of the organization (even if a direct relationship to a particular cost objective cannot be shown).
## Direct and Indirect Costs

<table>
<thead>
<tr>
<th>Direct Costs</th>
<th>Examples</th>
</tr>
</thead>
<tbody>
<tr>
<td>• Those costs that can be identified specifically with a particular final cost objective, i.e., a particular award, project, service, or other direct activity of an organization.</td>
<td>• EHS home visitor salary and fringe benefits.</td>
</tr>
<tr>
<td></td>
<td>• Bus to transport only Head Start children.</td>
</tr>
<tr>
<td></td>
<td>• Van used by EHS home visitors and LIHEAP home energy efficiency inspectors.</td>
</tr>
</tbody>
</table>
### Indirect Costs

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

### Examples

- **Facilities:**
  - Depreciation and use allowances on buildings
  - Shared common areas
  - Janitorial expenses
  - Maintenance expenses

- **Administrative**
  - Executive Director, Human Resources Manager, Chief Financial Officer salaries and fringe benefits
  - General liability insurance
  - Agency-wide telephone service
  - Rent for administrative offices
Must Comply with Cost Principles

The following cost principles apply to Head Start and Early Head Start grantees:

- **2 CFR 230** for non-profit organizations;
- **2 CFR 220** for colleges or universities;
- **2 CFR 225** for local government organizations, including Indian Tribal Governments; and
- **48 CFR Part 31** for commercial organizations.
Administrative and Development Cost Limitation

- Head Start Act Sec. 644(b): No financial assistance shall be extended under this subchapter in any case in which the Secretary determines that the costs of developing and administering a program assisted under this subchapter exceed 15 percent of the total costs, including the required non-Federal contributions to such costs, of such program.

- 45 CFR §1301.32. Limitation on Costs of Administration and Development of a Head Start Program.
Indirect Cost Rate

- *Indirect Cost Rate* means the ratio, expressed as a percentage, of an organization's total indirect costs to its direct cost base (includes non-Federal share).
- May be actual or negotiated by the grantee through the HHS cognizant Federal agency /Program Support Center: http://www.psc.gov/financial/cost_allocation/
  - 85% reviewed and negotiated within 180 days
  - 100% of proposals for first-time grantees reviewed within 90 days
Example: Negotiated Indirect Cost Rate and Development and Administrative Cost Limitation

Overall Program Funding Federal and Non-Federal

- Direct Costs: Dev and Admin – 10%
- Direct Costs: Other – 65%
- Indirect Costs: Dev and Admin – 5%
- Indirect Costs: Other (Facilities) – 21%

May not Exceed 15%

Negotiated indirect cost rate = 25%
### Most Common Cost Allocation Error

<table>
<thead>
<tr>
<th>Funding</th>
<th>Cost Allocation</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Budget</strong></td>
<td><strong>Building Use</strong></td>
</tr>
<tr>
<td>50% Head Start</td>
<td>25% Head Start</td>
</tr>
<tr>
<td>35% Early Head Start</td>
<td>25% Early Head Start</td>
</tr>
<tr>
<td>15% Private Pay</td>
<td>50% State Pre-school</td>
</tr>
</tbody>
</table>
Monitoring Cost Allocation

- Does the grantee have a written cost allocation plan?
- If no, does the grantee have a method of allocating costs which reflects the relative degree of benefit for all programs sharing in the allocated cost? Describe the program’s method of allocating costs.
  - Staff who have shared duties.
  - Shared facilities.
  - Shared equipment or busses (> $25,000).
Guidance from ECLKC


- Generally, the methods used to allocate a shared cost should be the simplest, most straightforward way of allocating this type of cost fairly.

- Complex, highly detailed methods should be avoided when a simple one will achieve the objective.
Cost Allocation Planning for Shared Staff
Considerations for Allocation of Staff

- Hours and days during which staff services are provided.
- Nature of the services.
  - Program-specific
  - General (e.g. administrative or facilities)
- Who (children, families, programs) benefits from the services?
- Also important for staff:
  - Adequacy of time records
  - Consistency with job descriptions
  - Reflected in payroll records
  - Confirmed by personnel activity reports
Children receive services for ten hours per day.
Head Start services are from 8 am – 4 pm.
State child care services are from 7 am – 8 am and from 4 pm – 5 pm.

- All children in the classroom are Head Start eligible.
- The same number of children attend throughout the day.
- The teacher and teacher assistant work the entire day from 7 am – 5 pm.
- The rates of pay for the teacher and teacher assistant are the same throughout the day.
- Both Head Start and child care services are offered five days per week.

How would you allocate teacher and teacher assistant staff costs?
<table>
<thead>
<tr>
<th>Time</th>
<th>Teacher HS</th>
<th>Assistant HS</th>
<th>Teacher CC</th>
<th>Assistant CC</th>
</tr>
</thead>
<tbody>
<tr>
<td>7 – 8 am</td>
<td></td>
<td>X</td>
<td>X</td>
<td></td>
</tr>
<tr>
<td>8 – 9 am</td>
<td>X</td>
<td></td>
<td></td>
<td>X</td>
</tr>
<tr>
<td>9 – 10 am</td>
<td>X</td>
<td></td>
<td></td>
<td>X</td>
</tr>
<tr>
<td>10 – 11 am</td>
<td>X</td>
<td></td>
<td></td>
<td>X</td>
</tr>
<tr>
<td>11 am – Noon</td>
<td>X</td>
<td></td>
<td></td>
<td>X</td>
</tr>
<tr>
<td>Noon – 1 pm</td>
<td>X</td>
<td></td>
<td></td>
<td>X</td>
</tr>
<tr>
<td>1 pm – 2 pm</td>
<td>X</td>
<td></td>
<td></td>
<td>X</td>
</tr>
<tr>
<td>2 pm – 3 pm</td>
<td>X</td>
<td></td>
<td></td>
<td>X</td>
</tr>
<tr>
<td>3 pm – 4 pm</td>
<td>X</td>
<td></td>
<td></td>
<td>X</td>
</tr>
<tr>
<td>4 pm – 5 pm</td>
<td></td>
<td>X</td>
<td></td>
<td>X</td>
</tr>
<tr>
<td>Hours Worked:</td>
<td>8/10=80%</td>
<td>8/10=80%</td>
<td>2/10=20%</td>
<td>2/10=20%</td>
</tr>
</tbody>
</table>
Support of Salaries and Wages

- **2 CFR Part 230 Appendix B: Section 8—Compensation for Personal Services**
  - See, in particular, subsection m. Support of salaries and wages.

- **Required for all employees:**
  - Documented payrolls approved by a responsible official of the organization.
  - Reports reflecting the distribution of activity of each employee for all staff members (professionals and nonprofessionals) whose compensation is charged, in whole or in part, directly to awards. In addition, in order to support the allocation of indirect costs, such reports must also be maintained for other employees whose work involves two or more functions or activities if a distribution of their compensation between such functions or activities is needed in the determination of the organization's indirect cost rate(s) (e.g., an employee engaged part-time in indirect cost activities and part-time in a direct function).
    - After-the-fact determination of activity for each employee.
    - Must account for the total activity for which employees are compensated and which is required in fulfillment of their obligations to the organization.
    - Must be signed by the individual employee, or by a responsible supervisory official having first hand knowledge of the activities performed by the employee.
    - Represents a reasonable estimate of the actual work performed by the employee during the periods covered by the reports.
    - The reports must be prepared at least monthly and must coincide with one or more pay periods.

- **Required for all nonprofessional (nonexempt) employees:**
  - Charges for the salaries and wages of nonprofessional employees, in addition to the supporting documentation described in subparagraphs (1) and (2), must also be supported by records indicating the total number of hours worked each day maintained in conformance with Department of Labor regulations implementing the Fair Labor Standards Act (FLSA) (29 CFR part 516). For this purpose, the term "nonprofessional employee" shall have the same meaning as "nonexempt employee," under FLSA.
Cost Allocation for Shared Facilities
Considerations for Allocation of Facilities

- Use floor plans, blueprints or measurements.
- Assign square footage to individual programs to the extent possible.
- Calculate percentages of shared use from assigned square footage.
- Apply percentages of shared use to square footage which can’t be assigned to individual program (common areas).
- Make sure all space is accounted for.
- May need to factor in amount of time used to equitably apportion shared space.
Example: The Sunshine Center

- The Sunshine Center building floor plan shows it to be 10,000 square feet, used as follows:
  - Head Start (HS) classrooms: 3,000 sq. ft
  - Offices for EHS home visitors: 2,000 sq. ft
  - Adult Basic Education (ABE) classrooms: 2,000 sq. ft
  - Meeting room: 1,000 sq. ft
    - Used 30 hours per week for ABE classes
    - Used 10 hours per week for EHS meetings
    - Not used by HS program
  - Common areas: 2,000 sq. ft
    - Stairways, halls, utilities, public restrooms used by all programs
      - How would you allocate rent and utilities for the Sunshine Center?
Sunshine Center Cost Allocation Plan

<table>
<thead>
<tr>
<th></th>
<th>Head Start</th>
<th>Early Head Start</th>
<th>Adult Basic Ed</th>
</tr>
</thead>
<tbody>
<tr>
<td>Classrooms</td>
<td>3,000</td>
<td></td>
<td>2,000</td>
</tr>
<tr>
<td>Offices</td>
<td></td>
<td>2,000</td>
<td></td>
</tr>
<tr>
<td>Meeting Room</td>
<td></td>
<td>250</td>
<td>750</td>
</tr>
<tr>
<td>• 30 hours ABE (75%)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>• 10 hours EHS (25%)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Subtotals:</td>
<td>3,000</td>
<td>2,250</td>
<td>2,750</td>
</tr>
<tr>
<td>Common Areas</td>
<td>750</td>
<td>560</td>
<td>690</td>
</tr>
<tr>
<td>Entire Center:</td>
<td>3,750</td>
<td>2,810</td>
<td>3,440</td>
</tr>
<tr>
<td>Total:</td>
<td></td>
<td></td>
<td>10,000</td>
</tr>
<tr>
<td></td>
<td>37.5%</td>
<td>28.0%</td>
<td>34.5%</td>
</tr>
</tbody>
</table>
Cost Allocation for Other Shared Assets & Services
Example: Busses and Vehicles

- The Head Start (HS) program shares a bus with the local school system.
- The bus transports both HS (10) and school aged children (20) in the morning.
- The bus makes a run at 2:00 pm with only the 10 HS children.
- The bus makes a run at 3:30 pm with only the 20 local school children.
- Each of the runs is 80 miles round trip.
- Bus operating costs are $1.32 per mile (driver and bus monitor not included).
### Bus Cost Allocation Plan

<table>
<thead>
<tr>
<th>Trip No.</th>
<th>Mileage</th>
<th>Head Start</th>
<th>Public School</th>
</tr>
</thead>
<tbody>
<tr>
<td>Morning Route</td>
<td>80</td>
<td>10</td>
<td>20</td>
</tr>
<tr>
<td>2:00 pm Route</td>
<td>80</td>
<td>10</td>
<td>None</td>
</tr>
<tr>
<td>3:30 pm Route</td>
<td>80</td>
<td>None</td>
<td>20</td>
</tr>
<tr>
<td><strong>Totals:</strong></td>
<td><strong>240</strong></td>
<td><strong>20</strong></td>
<td><strong>40</strong></td>
</tr>
<tr>
<td><strong>Percentage used:</strong></td>
<td>33.3%</td>
<td>66.7%</td>
<td></td>
</tr>
<tr>
<td><strong>Cost per Route:</strong></td>
<td>240 x $1.32 = $316.80</td>
<td>.333 x $316.80 = $105.50</td>
<td>240 x $1.32 = $316.80</td>
</tr>
</tbody>
</table>

- **Considerations for Allocation of Buses and Vehicles**
  - Reason for use of vehicle
  - Operating cost
  - Cost per mile
  - Number of passengers
  - Make-up of passengers
The agency has a contract to receive information technology (IT) support for all of its electronic equipment.

Under the contract, electronic equipment includes laptop and desktop computers, low volume printers and scanners.

The contract includes services to the Head Start, Early Head Start, Weatherization and RSVP Programs.

The agency maintains excellent property records.

The contracted amount is $20,000 per program fiscal year.
**IT Contract Cost Allocation Plan**

<table>
<thead>
<tr>
<th></th>
<th>Laptops</th>
<th>Desktops</th>
<th>Printers</th>
<th>Scanners</th>
<th>Total and Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Head Start</td>
<td>45</td>
<td>90</td>
<td>45</td>
<td>10</td>
<td>190</td>
</tr>
<tr>
<td>Early Head Start</td>
<td>50</td>
<td>10</td>
<td>5</td>
<td>5</td>
<td>70</td>
</tr>
<tr>
<td>Weatherization</td>
<td>65</td>
<td>20</td>
<td>20</td>
<td>10</td>
<td>115</td>
</tr>
<tr>
<td>RSVP</td>
<td>10</td>
<td>5</td>
<td>5</td>
<td>0</td>
<td>20</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>395</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

- **Considerations for Allocation of Services**
  - Consider allocation when negotiating the agreement
  - Address basis for calculating services
  - Amend agreement if needed to add or change programs and services
Review: Key Principals of Cost Allocation

- Define use of cost or service.
- Identify direct and indirect costs.
- Categorize and group costs and services.
- Choose allocation methods.
- Update regularly and as needed.
- Report monthly.
- Keep careful records.
- Review for currency and consistency.
Questions and Comments