

**SOUTH CAROLINA DEPARTMENT OF EDUCATION
2016–17 INDIRECT COST RATE PROPOSALS:
GENERAL INFORMATION**

Part I

In accordance with information received from the Secretary of Education and from the Office of Grant and Contract Financial Management, United States Department of Education, after July 1, 1973, local education agencies (LEAs) are required to have an approved indirect cost allocation proposal and rate in order to recover any indirect cost related to federal grants and contracts.

**UNIFORM ADMINISTRATIVE REQUIREMENTS, COST PRINCIPLES, AND
AUDIT REQUIREMENTS FOR FEDERAL AWARDS**

2 CFR, Part 200.400 sets forth the cost principles for determining the allowable costs of programs administered by state and local governments under the grants and contracts with the federal government.

The objectives of the principles are

- to establish uniform standards of allowability,
- to identify the full cost of federal programs,
- to ensure that federal programs bear their fair share of costs, and
- to simplify intergovernmental relations.

Applications for grants and contracts usually involve a request for reimbursement of both direct and indirect costs. Indirect costs are those that are not readily identifiable with the activities of the grant and contract but are, nevertheless, incurred for the joint benefit of those activities and other activities or programs of the organization.

Indirect costs are those meeting two criteria:

- they are incurred for a common or joint purpose benefiting more than one cost objective and
- they are not readily assignable to the cost objectives specifically benefited.

The following are some examples of services that typically benefit several activities and programs for which an indirect cost proposal may be used to attribute costs:

- accounting,
- auditing,
- budgeting,
- payroll,
- personnel, and
- purchasing.

In theory, all such costs can be charged directly. However, practical limitations and the consideration of efficiency in accounting preclude such an approach. 2 CFR, Part 200.400 was issued to provide uniform governmentwide principles for determination and reimbursement of indirect costs through the mechanism of an indirect cost rate.

Certain limitations on recovery of indirect costs exist:

- Federal law may limit the amount of indirect costs that may be recovered. For example, the maximum indirect cost allowable by law for a particular program may be less than the amount allowable under 2 CFR, Part 200.400. Certain programs such as the Title II Eisenhower Professional Development Program and Title I, for example, restrict payment to only those expenditures that “supplement, not supplant” local effort.
- Recovery of indirect costs is subject to availability of funds. If a combination of direct and indirect costs exceeds the amount of funds available, the LEA will not be able to recover the total cost of the project or program.
- Indirect costs may be recovered only to the extent that direct costs were incurred. The indirect cost rate is applied to the amount expended, *not to the total grant award*, in order to determine the amount for indirect costs.

If the indirect costs are determined but not claimed for the grant or contract, such amount may be used as “local effort” if local matching funds are required. Indirect cost proposals must be submitted annually for approval of new rates. LEAs are not required to develop an indirect cost allocation plan; however, if they fail to do so, they will not be allowed to recover any indirect costs related to federal grants and contracts.

INDIRECT COST PROPOSALS

The advantage of an indirect cost proposal and rate is that it is a simplified means for determining a fair share for indirect costs of federal grants and contracts that are acceptable to federal grantor agencies. The South Carolina Department of Education has, in cooperation with the United States Department of Education and representatives of school districts, developed indirect cost plans to be used by LEAs in South Carolina. The state of South Carolina has 81 LEAs and 61 charter schools. All charter schools are sponsored by a LEA and charter school data is blended with the LEAs to calculate the indirect cost rate for the LEA.

The State Superintendent of Education, or the State Superintendent’s designated representative, has been delegated the authority by the Office of Management and Budget to review indirect cost proposal data and to approve indirect cost rates for LEAs.

The South Carolina indirect cost plans for LEAs establish maximum fixed with carryforward rates for a given fiscal year. The LEA may elect to claim indirect costs at a rate less than the maximum.

The following two indirect cost allocations plans have been approved by the Office of Management and Budget for use by South Carolina school districts:

- a. the "Unrestricted Indirect Cost Proposal" (for use with grants and contracts that do not carry the "supplement, not supplant" language and
- b. the "Restricted Indirect Cost Proposal" (for use with grants and contracts that are subject to the "supplement, not supplant" legislative restrictions).

Audited expenditures for the second preceding fiscal year are to be used in the completion of the indirect cost proposals for a given fiscal year. Audited expenditures for fiscal year 2014–15 were used to compute the indirect cost proposals for fiscal year 2016–17. **Please note that the rates are fixed with carryforward provisions.**

It is essential that LEAs classify expenditures uniformly and consistently. *Types of expenditures identified as indirect costs shall not be included also as direct costs.* Similar types of expenditures must be consistently recorded to the same accounting class. All expenditures detailed on the audited financial report must have been made, and records supporting them must be maintained by the LEA. Generally, records and documentation supporting the indirect cost proposal must be retained for a period of five years after the last day of the fiscal year to which the plan applies. If audit exceptions have been noted, records will be retained until exceptions have been resolved.

The superintendent, the superintendent's secretary, and expenses related directly to the operation of the superintendent's immediate office, specifically, are not included in the restricted indirect costs. An individual principal, a principal's secretary, and the expenses related to the operation of these immediate offices are included in the base for the restricted indirect cost rates. These costs are included in the base for rate computational purposes.

Heads of Components (Head of Organizational Units)

Head of Component as defined in the U.S. Department of Education Cost Allocation Guide for State and Local Governments, September 2009, are treated as a direct cost. The U.S. Department of Education Cost Allocation Guide for State and Local Governments defines component costs as "...organizational units for both indirect and direct functions existing one level below the Chief Executive Officer unit." Also, "The grantee's organizational structure is considered in determining adjustments for components." LEAs should capture expenditures for the head of component (organizational) units in object codes 180, 281-289, 380, 480, and 680. However, LEAs whose 135-day ADM is 2,000 students or less may elect to maintain the current reporting treatment for the head of the component unit., There are approximately 17 LEAs with an ADM of less than 2,000 students. For example, if the head of the component is performing more management duties than actually

performing day-to-day operations, the head should be pulled out of the pool and charged to the base. As an example, the Chief School Financial Officer salary, benefits, travel, and other associated costs are treated as a direct cost for restricted rate calculations." **For indirect cost calculations, the head of a component unit does NOT include the head of an entity determined to be a component unit of a LEA such as a charter school or foundation.**

Subcontracts/Subawards

The indirect cost rate calculation should exclude subcontract/subaward expenditures exceeding \$25,000 and other distorting items. Subawards in excess of \$25,000 should be recorded to function 265. See "Excluded costs" section below.

Under subcontract/subaward agreements, the second-tiered entity receives funds (whether contract, grant or other agreement) from a prime recipient, to carry out a portion of a program. The entity works independently and is responsible for decision making.

The key, to determining whether the first \$25,000 of subcontracts/subawards should be included in the base, is the level of administrative/indirect expenses that benefit the subcontract/subaward activity. These types of activities (whether subcontract, subaward or vendor services) generally do not benefit from the administrative/indirect expenses to the same degree as other direct activities because items such as facilities, supplies, accounting services, administrative support and management, etc., are not provided to the same extent.

TERMINOLOGY

Indirect Cost Rate. An *indirect cost rate* is simply a device for determining, in a reasonable manner, what proportion of general expenses each federal grant or contract should bear. It is the ratio between total indirect costs and some direct cost base, commonly either direct salaries and wages or total direct costs, exclusive of any extraordinary or distorting expenditures such as capital outlay, major subcontracts, alterations, and renovations.

The indirect cost rate formula is as follows:

$$\text{INDIRECT COST RATE} = \text{INDIRECT COSTS} \div \text{DIRECT COSTS}$$

Excluded Costs. Certain items of costs are classified in 2 CFR, Part 200.400 as extraordinary or distorting expenditures and are excluded from the computation of the indirect cost rate because the activities require minimal administrative support. Once the indirect cost rate is calculated, it must be applied in the same manner as the calculation (consistency), therefore, the indirect cost rate should not be applied to any excluded or distorting items of costs."

Excluded costs in this category include Unused Leave Payments, Object Code 140; Capital Outlay, Function 253; Debt Service, Function 500 series; and Other Charges, Function 400 series. In addition, Food Services expenditures for food,

supplies, purchased services directly charged, and equipment charged to Function 256 have been excluded for the unrestricted rate and the restricted rate under instructions from the OMB. Subawards in excess of \$25,000 have also been excluded from the unrestricted and restricted rate.

Disallowed Costs. 2 CFR, Part 200.400 classifies certain items of cost as *disallowed*, which means that the federal funds cannot be used for these items. These are costs directly attributable to governance. For formula computational purposes, these governance costs are combined with direct costs.

Indirect Costs. *Indirect costs* are costs of a general nature. They are incurred for a common or joint purpose benefiting more than one activity specifically without effort disproportionate to the results achieved.

Direct Costs. *Direct costs* are those that are incurred specifically for one activity and that can be identified specifically with that activity. These costs may be charged directly to grants, contracts, and other programs against which costs are finally recorded.

Restricted Rate. In accordance with an advisory statement from the Secretary of Education, a *restricted* indirect cost rate must be applied to grants and contracts that contain the "supplement, not supplant" legislative restrictions. The restricted rate would apply in grant programs under the Elementary and Secondary Education Act, the Individuals with Disabilities Education Act, the Carl D. Perkins Vocational and Applied Technology Education Act, and any other legislative authority requiring assurance that federal funds will be so used to supplement and in no case to supplant state or local funds.

Excluded Costs

RESTRICTED RATE	UNRESTRICTED RATE
A. Facility Acquisition and Construction (Function 253)	A. Facility Acquisition and Construction (Function 253)
B. Food Services (Function 256, food and supplies)	B. Food Services (Function 256, food and supplies and object 393, food service direct purchased services)
C. Other Charges (Function 400 series, transfer expenditures)	C. Other Charges (Function 400 series, transfer expenditures)
D. Debt Service (Function 500 series)	D. Debt Service (Function 500 series)
E. Equipment (Object 540 series)	E. Equipment (Object 540 series)
F. Subawards in excess of \$25,000 (Function 265)	F. Subawards in excess of \$25,000 (Function 265)
G. Unused Leave Payments (Object Code 140)	G. Unused Leave Payments (Object Code 140)

Indirect Costs

RESTRICTED RATE

- A. Board of Education
(only Account 231-318, Audit
Services) *
- B. Fiscal Services (Function 252)
- C. Internal Services (Function 257)
- D. Internal Auditing Services (Function
259)
- E. Central Support Services
(Function 260 series, Except 261)

UNRESTRICTED RATE

- A. Board of Education
(only Account 231-318, Audit
Services) *
- B. Fiscal Services (Function 252)
- C. Operation and Maintenance of Plant
(Function 254)
- D. Internal Services (Function 257)
- E. Internal Auditing Services (Function
259)
- F. Central Support Services (Function 260
series)
- G. Depreciation or Use Allowance on
Buildings and Equipment

* In accordance with 2 CFR, Part 200.425, an entity may not charge audit costs to a federal award if the entity has total federal award expenditures of less than \$750,000 per year.

Direct Costs

RESTRICTED RATE	UNRESTRICTED RATE
A. Instruction (Function 100 series)	A. Instruction (Function 100 series)
B. Pupil Services (Function 210 series)	B. Pupil Services (Function 210 series)
C. Instructional Staff Services (Function 220 series)	C. Instructional Staff Services (Function 220 series)
D. Board of Education (Function 231 except Object 318, Audit Services)	D. Board of Education (Function 231 except Object 318, Audit Services)
E. Office of Superintendent (Function 232)	E. Office of Superintendent (Function 232)
F. School Administration (Function 233)	F. School Administration (Function 233)
G. Operation and Maintenance of Plant (Function 254)	G. Pupil Transportation (Function 255)
H. Pupil Transportation (Function 255)	H. Food Services (Function 256 except food, supplies, and equipment)
I. Food Services (Function 256 except food, supplies, equipment)	I. Supporting Services Pupil Activity (Function 271)
J. Head of Component (Organizational) Units (Function 261)	J. Community Services (Function 300 series)
K. Heads of Component (Organizational) Units (Objects 180, 281-289, 380, 480, 580, 680)	K. Summer School (Function 170 series)
L. Supporting Services Pupil Activity (Function 271)	
M. Community Services (Function 300 series)	
N. Summer School (Function 170 series)	

SUBMITTING THE INDIRECT COST PROPOSAL

An e-mail with your LEA's indirect cost proposal has been submitted to you. Please review the proposals carefully. If you agree with the data entered and calculated, please sign, scan, and return the delegation agreement via e-mail to auditing-services@ed.sc.gov. If revisions need to be made, please e-mail us a copy back noting the areas of concern. If changes are necessary, a copy of the approved proposals will be sent to the office of your district superintendent by the South Carolina Department of Education.

APPLYING THE INDIRECT COST RATE

The indirect cost rate is necessary in order to compute the indirect cost dollar amounts. The LEA is required to use the approved rate in all applications for federal grants during the fiscal year for which the rate has been established. (As noted above, separate rates are established for unrestricted programs, restricted programs, and the food service program.) The indirect cost dollar amount (**I**) is the product of the indirect cost rate (**R**) multiplied by the direct cost dollar amount (**G**).

Therefore **(I) = (R x G)**

A. Determining Total Current Expenses

Total current expenses (**TCE**) equals the sum of the indirect cost dollar amount (**I**) plus the direct cost dollar amount (**G**).

Therefore **(TCE) = (I) + (G)**

B. Determining the Fixed Grant Amount

Total federal award equals the sum of the total current expenses (**TCE**) plus expenses for the following account classifications:

- Facility Acquisition and Construction, Function 253;
- Debt Service, Function 500 series; and
- Other Charges, Function 400 series.

C. Determining Indirect Cost Dollar Amounts for Restricted Programs

As shown above, the formula for the indirect cost dollar amount is **I** (indirect cost dollar amount) = **R** (indirect cost rate) **x G** (direct cost dollar amount).

In entitlement programs such as the Title I, Basic State Grant Programs, the indirect cost rate would be established on the basis of the 2nd preceding year financial data for all appropriate expenses. This value **R**, after approval by the South Carolina Department of Education, would be used in the formula.

To determine **I** (the *indirect cost* dollar amount) and **G** (the *direct cost* dollar amount), you must first identify the total entitlement or fixed grant amount already established by the award.

From this dollar amount, subtract costs computed for Facility Acquisition and Construction (**C**), Debt Service (**D**), and Other Charges (**T**). The remainder is the sum of the indirect cost dollar amount (**I**) and the direct cost amount (**G**).

For simplicity of the formula, assume an indirect cost rate (**R**) of 2.5 percent (.025) and give the direct cost dollar amount (**G**) its value of 100 percent (1.000) as representing the total direct costs.

Example

Fixed grant amount	\$927,000
Less	
Facility Acquisition and Construction (C)	-\$23,000
Debt Service (D)	-\$3,000
Other Charges (T)	<u>-\$1,000</u>
Sum of indirect cost and direct cost (I + G)	\$900,000
Indirect cost rate (R + 100% direct costs, .025 + 1.00).....	1.025
Direct cost dollar amount (\$900,000 ÷ 1.025)	
G = (I + G) ÷ (R + 100% direct costs)	\$878,049
Indirect cost dollar amount (.025 x \$878,049)	
I = RG	\$21,951

D. Determining Indirect Cost Dollar Amounts for Restricted Competitive Grant Programs

In a restricted ("supplement, not supplant") competitive grant program or contract, the indirect cost amount (**I**) is computed as it is in other programs. For example, in the equation **I = R** (indirect cost rate) **x G** (direct cost dollar amount), **G** is a known quantity, and after the indirect cost rate (**R**) is computed, the indirect cost dollar amount is derived directly from the **I = RG** formula. The total federal grant or contract amount for a restricted competitive program equals the sum of the direct costs, indirect costs, Facility Acquisition and Construction, Debt Service, and Other Charges.

E. Carryforward Computation

LEAs will use a fixed rate with a carryforward provision. A fixed rate with carryforward provision has characteristics of both a provisional rate, which is a temporary rate subject to adjustment, and a predetermined rate, which is a permanent rate not subject to adjustment. A rate is computed and fixed for a specified future period based on an estimate of that future period's level of operations. However, when the actual costs of that period become known, the difference between the estimated costs and the actual costs is carried forward as an adjustment to a subsequent period for which a rate is established. The adjustment cannot be made in the fiscal period immediately following because the fixed rate for the immediately following fiscal period will already have been determined. An adjustment generally will be carried forward to the second fiscal period following the period being adjusted. A fixed rate should be selected that will closely approximate the actual rate expected to be incurred. An accurate forecast will confine carryforward amounts to minimal differences. The following is a sample of a fixed with carryforward rate computation:

**South Carolina Department of Education
Office of Auditing Services
Sample Carryforward Computation**

		<u>INITIAL YEAR</u>	<u>SUBSEQUENT YEARS</u>	
		FY 2013	FY 2015	FY 2017
(a) FIXED RATE AS NEGOTIATED				
(B/A) - Computed as follows:		<u>5.3%</u> (C)	<u>4.0%</u> (C)	<u>5.6 %</u> (C)
Direct/Disallowed Costs		<u>\$106,995,436</u> (A)	<u>\$110,550,600</u> (A)	<u>\$114,100,980</u> (A)
Indirect cost pool:				
Indirect Costs		\$5,692,672	\$5,150,000	\$5,111,108
Fixed-Carry Forward (FCF)		<u>\$ 0</u>	<u>(\$709,182)</u>	<u>\$546,979</u>
Total Pool		\$5,692,672 (B)	\$4,440,818 (B)	\$5,657,997 (B)
(b) ACTUAL COSTS NEGOTIATED:				
Actual Direct/Disallowed Costs		\$110,550,600 (D)	\$114,100,980 (D)	
Actual Indirect Costs		\$5,150,000	\$5,820,200	
FCF		<u>\$ 0</u>	<u>(\$709,182)</u>	
Total Pool		<u>\$5,150,000</u> (F)	<u>\$5,111,018</u> (F)	
(c) CARRYFORWARD COMPUTATION:				
Indirect Eligible for Recovery (C*D):				
Fixed rate x Actual Direct/Disallowed Base:				
2013		\$5,859,182 (E)		
2015			\$4,564,039 (E)	
Should have recovered:				
Actual Indirect Costs for:				
FY 2013		<u>\$5,150,000</u> (F)		
FY 2015			<u>\$5,111,108</u> (F)	
UNDER OR (OVER) RECOVERY (F-E), CARRYFORWARD TO SUBSEQUENT YEAR		<u>(\$709,182)</u>	<u>\$546,979</u>	

* This is a sample only and is not intended to prescribe methods of charging costs.

SPECIAL INSTRUCTIONS

Part II

This plan has been designed to conform to the statewide financial accounting system utilized by all South Carolina school districts. You should review the following specific information prior to checking the indirect cost proposals:

- A. Verify expenditures to your FY 2014-15 audited data. Please note that if your district has a component unit, your component unit totals are included in the district's totals.
- B. Depreciation and allowance for the use of buildings, capital improvements, and equipment is employed in computing the unrestricted rate. This computation is based on the actual cost. However, where actual cost records have not been maintained, a reasonable estimate of original acquisition cost may be used. The computation will exclude any portion of cost donated or borne directly or indirectly by the federal government.
 - The cost of land also is excluded. When the depreciation method is used, adequate property records must be maintained. Any generally accepted method must be consistently applied for any specific asset or class of assets.
 - In lieu of depreciation, you may use an allowance for buildings and improvements computed at an annual rate of 2 percent and for equipment at an annual rate of $6\frac{2}{3}$ percent.
 - Depreciation or use allowance on idle or excess facilities is not allowable.
 - The information for depreciation and use allowance is submitted on the Supportive Information Sheet that is due annually by *December 1* with the submission of your annual audit report.
- C. Check your indirect cost proposals carefully. Sign the certification statement and return to

auditingervices@ed.sc.gov

A certified and approved copy of each proposal will be returned to you. If there are any errors, please make corrections on the proposals prior to submission.