Guidebook for Financial Managers
of Discretionary Grants

INTRODUCTION

This manual is intended to serve as an additional reference tool and guidebook for financial managers, program directors, and others responsible for the administration and financial management of federal discretionary grants (such as Head Start, Early Head Start, State Collaboration, Runaway & Homeless Youth grants, etc.).

The purpose of this guidebook is to explain and clarify federal regulations and existing policies in a straightforward manner, eliminating as much "government-ese" as possible along the way.

Copies of all the applicable federal financial management regulations (45 CFR Parts 74 and 92), federal cost principles (Office of Management and Budget [OMB] Circulars A-122, A-87, and A-21), and audit requirements (OMB Circular A-133), are available from this website.

Copies of all other documents cited, such as information memorandums, program instructions, and other small documents, are available by contacting your ACF Program Representative or the Regional Grants Officer.

It is our intention to periodically up-date the material in this manual as regulations and program legislation change. We also recognize that some things may have been left out, or need to be clarified. It's even possible you might feel we have made a mistake in our explanations of some policies. Because of this, we invite and welcome any and all comments on the information contained in this manual.

Please send your comments to me at the following address:

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Table of Contents

NOTE: Contact your program representative for documents marked as “exibits”.

<u>Section</u>

CHAPTER 1

GRANT APPLICATIONS AND AWARDS

1.01 GRANT APPLICATIONS
1.02 GRANT AWARDS
1.03 TERMS AND CONDITIONS OF AWARD

1.01 GRANT APPLICATIONS

Application forms and instructions for filing applications may be obtained from the ACF/Region VI program office authorized to fund the project. The filing instructions will also include information concerning deadlines for submission of applications, the mailing address, and a checklist of all required documents.

- **Competitive applications** are those submitted in response to an announcement of the availability of federal funds to support new projects, or sometimes to support a new sponsor for an existing grant. The announcements, usually published in the *Federal Register*, describe the program, and state the amount of funds available, the eligibility requirements, where to obtain application forms, the deadlines for submitting applications, etc. If competition is limited to a specific type of organization or a certain geographical area, the announcement may be made by publishing a notice in the *Federal Register*, mailing individual letters to all prospective applicants, publishing notices in local newspapers, and other suitable forms of public notice.
- **Non-competing continuation applications** are those submitted annually by existing grantees in order for a grant to be continued for the following budget period (but within the overall established project cycle), and are generally referred to as "refunding applications." For example, Early Head Start grantees submit refunding applications for each annual budget period within their 5 year project cycle. Annual refunding application forms for each new budget period will be mailed by ACF to the authorized grantee official (usually the Board Chairperson) approximately 6 months before the new budget period begins. If refunding application forms are not received by the grantee at the proper time, it is the responsibility of the grantee to request them from the ACF program office.

  The grantee should complete the refunding application for the new budget period, and then submit the original (signed by the authorized grantee official) and 2 copies to ACF no later than 3 months (90 days) before the new budget period begins. This will give ACF program staff time to review the refunding application, negotiate any necessary budget changes with the grantee, obtain any additional information necessary, and process the refunding award action before the new budget period begins and without any break in program services.

  Head Start grantees should input their refunding information on the PCCOST data diskette, check to ensure the data is correct, and then submit the diskette along with the paper copies of the application to ACF. (If you do not have a PCCOST data diskette, or have difficulty inputting the information on the diskette, contact your ACF Program Representative for assistance.)

- **Supplemental applications** are those submitted by existing grantees during the approved project period to request support for new or additional activities not identified in the current grant. For example, new funds generally become available each year for Head Start grantees, to give cost of living increases to their staff and to make program improvements, which require supplemental applications in order to receive the funds.
- **Budget revisions** may also require the submission of revised applications, depending on the nature and scope of the revision, as required by federal regulations 45 CFR 74.25 and 45 CFR 92.30. Further information related to budget revisions is in Chapter 9, "Prior Approvals."

1.02 GRANT AWARDS

When a grant award is approved and funded, ACF will send the grantee a "Financial Assistance Award" (FAA) document. A sample FAA is shown at the end of this chapter as Exhibit 1.1 for your reference.

The FAA states:

- the assistance type being awarded [Block 2];
- the grant award number [Block 3];
- the budget period being funded [Block 8];
- the overall project period [Block 9];
- the approved budget line items [Block 16];
- the non-federal share matching amount the grantee is required to provide [Block 17];
- the amount of federal funds being awarded by this action [Block 19];
- the grantee’s Employer Identification Number (EIN) [Block 22];

- the "Client Population" (meaning the number of children to be served), the specific federal program regulations, and other remarks specific to the terms of the award [Block 26].

It is important that grantees be aware that the FAA, along with the approved grant application, constitutes the legal definition of the grant program for purposes of financial management and compliance with grants management requirements stated in the Code of Federal Regulations, Parts 74 and 92. Auditors use the FAA and the approved application in determining compliance with federal requirements related to the grant, regardless of the source of the funds (federal or non-federal).

Attached to the initial FAA awarding grant funds will be a one-page document titled "Instructions for Requesting Payment of Federal Funds Awarded" [Exhibit 1.2], which includes a telephone number to contact the HHS/Payment Management System in order to set up an account and start drawing grant funds. Further information on how to draw down grant funds is in Chapter 2, "Grant Payments/Drawdowns and Interest."

1.03 TERMS AND CONDITIONS OF AWARD

- **Standard Terms and Conditions.** Also attached to the FAA, should be the two-page "Standard Terms and Conditions" [Exhibit 1.3] of the award. The Terms and Conditions document references the applicable federal financial and administrative regulations that must be followed, in Items #1 through #4 (in addition to the program regulations cited directly on the FAA in Block 26).

  Special attention should also be paid to Item #5, which states that the grantee must carry out the program in accordance with the approved application and any amendments to the application.

  Item #6 states that failure to submit required reports on time may be the basis for ACF withholding grant funds, or even terminating the grant. Further information related to financial reports is in Chapter 13, "Financial Reports."

  Item #8 states that obligations must be liquidated within 90 days after the end of the budget period, and that an unobligated balance of federal funds in one budget period does not authorize the grantee to use those funds in the following budget period. Further information on this subject is in Chapter 4, "Period of Availability of Funds."

- **Facility Terms and Conditions** apply whenever the grantee receives an FAA approving the purchase or construction of a facility with federal grant funds. A copy of the Facility Terms and Conditions [Exhibit 1.4] will be attached to the FAA that approves the award of funds for purchasing or constructing the facility. In particular, these conditions require grantees to record a Notice of Federal Interest in the property, so a sample format for the Notice is also included. Further information regarding facilities is in Chapter 12, "Facilities."

- **Special award conditions** may be imposed by ACF, in accordance with 45 CFR 74.14 and 92.12, if a grantee:

  (a) has a history of poor performance;

  (b) is not financially stable;

  (c) has a management system that does not meet the financial management standards prescribed;

  (d) has not conformed to the terms and conditions of a previous award; or

  (e) is not otherwise responsible.

There are various types of "special conditions" that may be imposed, depending on the grantee's situation. For example, financial status reporting might be required to be more frequent, or the grantee might be placed on reimbursement payment status (instead of the usual advance payment status). If special award conditions are imposed, they will be fully explained to the grantee, either in the "Remarks" section of the FAA, or in a separate letter.

CHAPTER 2

GRANT PAYMENTS/DRAWDOWNS AND INTEREST

2.01 GENERAL INFORMATION

A. Grantees will be notified of the prescribed payment method on the Financial Assistance Award (FAA) document. Payments will be made in accordance with federal regulations at 45 CFR 74.22 and 92.21. Generally, grant funds will be drawn down in advance on an as-needed basis from the HHS/Payment Management System (PMS), and direct-deposited in the grantee’s bank account, using either "Cashline" or "SmartLink." (See Exhibit 1.2, "Instructions for Requesting Payment of Federal Funds Awarded" and Exhibit 2.1, "Payment Management System.")

B. For nonprofit organizations and universities: when requesting information from PMS on payment information, confirmation of draw downs, and status of accounts, the request should be addressed to: Chief, Recipient Financing and Cash Management Branch II, Division of Payment Management, P.O. Box 6021, Rockville, Maryland 20852.

C. For State & local governments, including federally recognized Indian Tribes: when requesting information from PMS on payment information, confirmation of draw downs, and status of accounts, the request should be addressed to: Chief, Recipient Financing and Cash Management Branch I, Division of Payment Management, P.O. Box 6021, Rockville, Maryland 20852.

2.02 EMPLOYER IDENTIFICATION NUMBER (EIN)

A. All ACF grantees must have an Employer Identification Number (EIN) recorded in HHS's on-line Central Registry Subsystem (CRS) before payments can be processed by PMS. (The EIN is the identification number issued to organizations by the Internal Revenue Service.) A payee identification number (PIN) will also be assigned to the grantee by PMS as a unique identifier for each organization, to be used when drawing down grant funds.

B. Grantees are responsible for reporting to ACF any subsequent changes to their EIN, so that ACF can submit the new information to CRS. For applicants approved for funding, that do not have a unique identifying number already established in CRS, ACF must submit the EIN to CRS.

2.03 STEWARDSHIP OF GRANT FUNDS

A. As stated in federal regulations 45 CFR 74.22 and 92.21, grantee accounting and payment methods must minimize the time elapsing between the date when advance grant funds are requested (i.e., cash advance drawn down) from PMS and the date checks are disbursed to pay grant expenditures.

The regulations also state that cash advances to grantees:

- should be limited to the minimum amounts needed;
- should be timed to pay only the actual, immediate cash requirements of the approved grant program; and
- the timing and amount of cash advances should be as close as administratively feasible to the actual disbursements by the grantee for direct program costs (and the program's proportionate share of any allowable indirect costs).

This means that, for example, grantees should only draw down sufficient funds every pay period to pay the net payroll, not the total gross payroll. The remaining funds should only be drawn down a few days before each of the actual checks are disbursed for unemployment compensation, state taxes, employee pension plan contributions, insurance, etc.

B. Grantees are allowed to draw down grant funds as often as needed, daily in fact. But grantees are not to draw down any more than the actual, immediate needs of the program, and not to draw down grant funds from one program, in order to pay expenses of another program. As stated in the federal cost principles [OMB Circulars A-122, A-87, and A-21], using grant funds from one program to pay the costs of another program is not allowable.

Also, as stated in ACF-IM-91-10 [Exhibit 6.2], "Head Start grantees may not loan funds from Head Start to compensate for delayed or late payment from other funding sources. Costs allocated to non-Head Start funding sources may not be paid out of the Head Start budget, even on a temporary basis." (Further information may be found in Chapter 4, "Allowable Costs" and in Chapter 6, "Cost Allocation.")

C. In order to determine how much to draw down, most grantees determine the total of their accounts payable to be paid that week (and the net payroll to be paid out, if it is a payday week) and that is the amount of funds they request to draw down. One of the monitoring methods used by ACF and by grantee auditors is to compare monthly expenditures to monthly grant funds drawn down to see if they match reasonably.

D. Also, grantees should disburse funds available from repayments to and interest earned on a revolving fund, program income, rebates, refunds, contract settlements, audit recoveries, and interest earned on such funds <u>before</u> requesting additional cash payments.

E. ACF is responsible for monitoring the cash management practices of grantees in order to ensure that federal cash is not maintained in excess of that required for immediate disbursement needs, and to ensure grantees do not draw down funds for purposes other than to pay immediate program expenses.

2.04 PAYMENT SYSTEMS AND METHODS OF PAYMENT

There are four possible methods of payment available to ACF grantees. Listed below is a description of each:

1. **Treasury Check Advances:** When new grantees receive payments through PMS, they will usually be paid through advance by Treasury Check method. PMS provides the new grantee with instructions for requesting payments. Payments will be based on the submission of SF-270, Request for Advance or Reimbursement.

2. **Treasury Check Reimbursement:** If ACF determines that the grantee has not demonstrated the willingness and ability to maintain procedures that minimize the time elapsing between the transfer of funds from PMS and disbursement by the grantee, then ACF may request PMS to put the grantee on a Reimbursement by Treasury Check payment method. ACF may also use this method with grantees designated as "High Risk" or "Seriously Deficient" status.

3. **Cashline:** Although new grantees are generally first put on the Treasury Check method of payment (either advance or reimbursement), PMS works with the grantee, to arrange payment by "Cashline" or "SmartLink" (described below), as soon as possible.

<u>"Cashline"</u> allows the grantee organization using any touch-tone telephone to dial directly into a "Voice Response" computer located in Rockville, Maryland to request funds as frequently as necessary. The funds can then be electronically deposited on the next business day after requesting funds at the financial institution of their choice, or be mailed via Treasury Check to the grantee within a week. PMS provides grantees with instructions on accessing funds through this system. The Cashline payment method enables the grantee to withdraw Federal cash as frequently as disbursements are made. Since funds are available the next business day, it is not necessary for grantees to maintain any sizeable balances of Federal cash on hand when using this payment method.

4. **SmartLink:** <u>"SmartLink"</u> is an electronic transfer system that can be accessed through the grantee's computer terminal. PMS provides instructions to grantees on procedures for accessing funds through this system. This system offers the same advantages as Cashline for the grantee by allowing them to withdraw funds on a daily basis if necessary.

2.05 REQUESTING ADVANCES OR REIMBURSEMENT FROM PMS

A. **Request for Advance:** Grantees requesting advance by Treasury check (rare in our region) through PMS will receive appropriate forms and instructions from PMS shortly after notification of award. Payment requests should generally be made on a monthly basis and submitted on form PMS-270. In no case may they be submitted more frequently than monthly.

All grantees are required to submit form PMS-272, "Federal Cash Transaction Report" quarterly to PMS. This report is used by PMS to obtain disbursement or outlay information for each grant and is to be submitted no later than 15 working days following the end of each quarter.

B. **Request for Reimbursement:** For grantees paid on a reimbursement basis, the PMS-270 must be submitted to the ACF Regional Grants Officer for review and approval before forwarding to PMS. This method allows the Grants Officer to closely monitor the grantee's actual cash disbursements. The grantee may submit its request for reimbursement monthly and may submit more often if authorized.

C. **Cashline:** Grantees paid by Cashline follow the same procedures as above for advance payment, however, the payment is processed by PMS through electronic transfer via the telephone, rather than a check, and the grantee has access to the money the next business day. Requests for funds may be made on a daily basis, if necessary.

D. **SmartLink:** Grantees paid by SmartLink follow the same procedures as those for Cashline, however, the payment is processed by PMS through electronic transfer via a computer, rather than the telephone. The grantee has access to the money the next business day, and requests for funds may be made on a daily basis, if necessary.

2.06 WITHHOLDING OF PAYMENTS

A. ACF may request PMS to withhold payments when the grantee has failed to comply with reporting requirements, owes money to the federal government, is suspended or terminated, or otherwise has violated the terms and conditions of its award.

B. Also, when a grantee owes a debt that is to be collected, ACF may withhold grant payments, or offset the debt against current grant funds and require the grantee to repay it to the program using non-federal funds.

2.07 INTEREST EARNED ON FEDERAL GRANT FUNDS

Separate bank accounts for federal grant funds are not generally required, but the grantee must be able to account for the receipt, obligation, and expenditure of grant funds. Advances of federal funds must be deposited and maintained in insured accounts whenever possible.

In addition, non-profit grantees must maintain advances of federal funds in interest-bearing accounts, unless one of the following conditions apply:

- the grantee receives less than $120,000 in federal awards per year;
- the best reasonably available interest-bearing account would not be expected to earn interest in excess of $250 per year on federal cash balances; or
- the bank would require an average or minimum balance so high that it would not be feasible within the grantee's expected federal and non-federal cash resources.

Interest earned on federal advances deposited in interest-bearing accounts must be remitted annually to PMS via the PMS-272 report. For non-profit organizations, the first $250 of interest earned per year may be retained by the grantee for administrative expense, and so should not be reported by the grantee on the PMS-272 form. For governmental organizations, only the first $100 of interest earned per year may be retained for administrative expenses.

CHAPTER 3

FINANCIAL MANAGEMENT STANDARDS

3.01 <u>GENERAL FISCAL CONTROLS</u>

Grantee fiscal controls and accounting procedures must be sufficient to:

permit preparation of required federal reports (and provide supporting documentation for each of the figures on those reports); and

permit the tracing of grant funds to a level of expenditures adequate to establish that such funds were used properly (i.e., funds were not used in violation of the restrictions of the regulations governing the grant, including program regulations, and financial and administrative regulations).

Each grantee is permitted to establish its own accounting system, in whatever manner it feels is best suited to its particular organizational structure, <u>provided</u> that it is based on sound accounting principles and meets the federal standards for grantee financial management systems.

3.02 <u>STANDARDS FOR FINANCIAL MANAGEMENT SYSTEMS</u>

Federal regulations at 45 CFR 74.21 and 92.20, state that grantees' financial management systems must meet the following standards:

A. **Financial reporting.** Accurate, current and complete disclosure of the financial results of each program must be made, in accordance with the federal financial reporting requirements, for each of the ACF grants. This includes the Financial Status Reports (SF-269) sent to the ACF Regional Office, as well as the Cash Transaction Reports (PMS-272) sent to the HHS/Division of Payment Management.

The amounts reported by grantees on their SF-269's and PMS-272's should be readily traceable back to their accounting records. (See federal regulations 45 CFR 74.52 and 92.41, and Chapter 13 "Financial Reports," for further information.)

B. **Accounting records.** Records must be maintained (1) that adequately identify the source and application of funds provided for financially assisted activities, and (2) which contain information pertaining to federal awards, authorizations, obligations, unobligated balances, assets, outlays or expenditures, liabilities, income and interest. The grantee's accounting records must include not only expenditures of federal funds, but also non-federal share matching. The accounting records must also include the grant obligations and liabilities.

C. **Internal control.** (1) Effective control over, and accountability must be maintained for all funds, and for all real and personal property and other assets; (2) grantees must adequately safeguard all such assets; and (3) grantees must assure that the assets are used solely for authorized purposes. (Internal financial management controls are discussed further in Chapter 16 "Internal Controls.")

D. **Budget control.** Actual expenditures or outlays must be compared with budgeted amounts for each grant. Grantees generally produce monthly budget comparison reports which compare budgeted line item amounts with monthly expenditures and expenditures for the grant year to-date. The reports also indicate the current balance remaining for each budgeted line item. Grantee program and administrative management staff then use this information each month to effectively manage each of their programs.

E. **Cash management.** Written procedures must be followed for minimizing the time elapsing between the transfer of funds to the grantee from the HHS/Payment Management System (PMS) and the issuance of checks for program purposes by the recipient, whenever advance payment procedures are used. (When advances are made by electronic transfer of funds methods, the grantee must make drawdowns as close as possible to the time of making disbursements. Grantees must also monitor cash drawdowns by their delegates to assure that they conform substantially to the same standards of timing and amount as apply to advances to the grantees.). See Chapter 2 "Grant Payments/Drawdowns and Interest" for more information.

F. **Allowable cost.** Written procedures must be followed for determining the reasonableness, allocability, and allowability of costs in accordance with the provisions of the applicable federal cost principles (OMB Circulars A-21, A-87, and A-122) and the terms and conditions of the award. See Chapter 4 "Allowable Costs" for more information.

G. **Source documentation.** All accounting records, including cost accounting records, must be supported by source documentation, such as cancelled checks, paid bills, payrolls, time and attendance records, contracts, delegate agency agreements, etc. In addition, the source documentation should be dated, and contain all required approval signatures and authorizations. See Chapter 16 "Internal Controls" and Chapter 14 "Records Retention" for more information.

3.03 <u>REVIEWS OF GRANTEE FINANCIAL MANAGEMENT</u>

ACF is responsible for monitoring grantee stewardship over federal funds. In accordance with the regulations, the ACF Regional Office may review the adequacy of the financial management system of any grantee at any time subsequent to award, or as part of a pre-award review.

As part of the Head Start grants, and Early Head Start grants, tri-annual PRISM reviews (previously OSPRI), ACF uses a 7-page "Fiscal Checklist" to determine how grantees are handling financial management of their programs, and whether the program services are being affected adversely because of the financial management.

ACF also performs tri-annual reviews of the Runaway and Homeless Youth grantees, called Peer Monitoring Reviews, which include review of grantee financial management.

In addition to these mandated reviews, our region also performs targeted on-site reviews of grantee financial management whenever we deem it necessary, for example based on audit findings (particularly repeat findings), or information from the public or news media, or congressional inquiries.

CHAPTER 4

ALLOWABLE COSTS

4.01 <u>COST ANALYSIS</u>

The ACF Regional Office performs a cost analysis on each application received for federal funds. The purpose of a cost analysis is to determine whether the costs proposed for a program are necessary, reasonable, allocable to the program, and allowable based on the applicable federal cost principles (OMB Circulars A-21, A-87, and A-122) and program regulations.

ACF analyzes the costs identified in the "Budget Information - Non-Construction Programs" sections of the SF-424, <u>Application for Financial Assistance,</u> using the narrative budget justification portion of the application, and any other resources available or requested by ACF.

The basis for determining allowability and allocability of costs charged to ACF grants is found primarily in the federal cost principles, listed in 45 CFR 74.27 and 92.22:

- Non-profit organizations (such as single-purpose Head Start agencies, and Community Action Agencies) use OMB Circular A-122;
- State, local, and tribal governments (such as cities, parishes, and public school boards) use OMB Circular A-87; and
- Institutions of higher education (such as colleges and universities) use OMB Circular A-21.

Each grantee is subject to only one set of cost principles, according to the type of organization it is. A sub-grantee (or delegate agency), receiving funds under an ACF grant, is subject to the cost principles applicable to its type of organization, which may not necessarily be the same as that of the grantee.

<u>All</u> ACF grant costs, including federal and non-federal share, are subject to the cost principles prescribed. Grantee organizations should consult the appropriate cost principles for specific guidance on allowable and unallowable costs, and should consult with the ACF Regional Office if they have questions concerning the allowability or treatment of a particular cost item.

Each set of cost principles (A-21, A-87, and A-122) lists in alphabetical order, a large number of different types of cost, and states whether each cost is allowable, unallowable, or allowable but with restrictions (such as prior approval requirements, justification of need, etc.). Copies of each of these OMB Circulars are located at the end of this manual.

4.02 <u>DETERMINATION OF ALLOWABILITY</u>

A cost is allowable if it is (a) reasonable; (b) allocable to the project for which the grant is awarded; (c) necessary for proper and efficient administration of the proposed project; (d) consistently treated as a direct or indirect cost; (e) permitted under the appropriate cost principles prescribed in 45 CFR 74.27 and 92.22; (f) not restricted or prohibited by the terms and conditions of the grant; and (g) in accordance with generally accepted accounting principles (GAAP).

Costs for which prior approval is required are not allowable unless they are included in the approved grant budget or are approved by the responsible ACF official in a subsequent written authorization.

4.03 <u>DETERMINATION OF REASONABLENESS</u>

As a general rule, a cost is reasonable if: (a) it does not exceed that which would be incurred by a prudent individual or organization under the circumstances prevailing at the time the decision was made to incur the cost; and (b) it is necessary for the performance of the grant project.

4.04 <u>DETERMINATION OF ALLOCABILITY</u>

Costs may be allocated to a grant supported project if they benefit the project either directly or indirectly. "Direct costs" are those which are specifically incurred for the project. "Indirect costs" are those which are necessary for the operation of the organization, but are not incurred specifically for any one project or program. Chapter 6 "Cost Allocation" discusses this in much greater depth.

4.05 <u>DETERMINATION OF CONSISTENT TREATMENT</u>

Costs must be consistently treated in accordance with the organization’s established accounting system without regard to the source of funds supporting the expenditures. This means that a cost cannot be allocated to one funding source using an approved indirect cost rate, and the same cost then be allocated to a different funding source using direct cost allocation methods. For example, building space costs could not be allocated to one funding source using an indirect cost rate, and to another funding source using a direct cost allocation method, such as square footage.

4.06 GENERALLY ACCEPTED ACCOUNTING PRINCIPLES

Generally accepted accounting principles (GAAP) direct how and when costs should be recognized on accounting records and financial statements. The federal cost principles (i.e., OMB Circulars A-122, A-87, and A-21) require the use of GAAP so that allowable costs can be based on procedures that are uniform. Questions about GAAP, and whether your accounting system meets GAAP requirements should be directed to your auditor, in fact, some grantees include such questions as part of their audit contracts.

4.07 DETAILED REVIEW OF SPECIFIC COST CATEGORIES

A number of Head Start grantee program and finance staff, as well as Policy Council and Board members, have asked for more information regarding how they should analyze various cost line items, prior to approving the grantee budget application and sending it to the ACF Regional Office. Listed below are a few line items and information regarding how our ACF staff generally review these cost categories.

A. Analysis of Personnel Costs (Salaries and Wages)

Personnel costs are allowable to the extent that they are reasonable and that the amount estimated is the same as the rate paid by the applicant under its established organizational wage and salary schedule. Further, wage and salary rates should be commensurate with rates paid for similar work in the labor market in which the organization competes for employees.

ACF determines whether salary costs included in this budget category are direct costs or indirect costs. This is generally accomplished by reviewing the indirect cost rate negotiation agreement to determine if the types of salary costs identified in the budget have been included in the indirect cost pool. Questionable items which cannot be resolved with the information in the agreement will be checked with the Regional Division of Cost Allocation (RDCA).

A review of the program narrative will be done to determine that the number of staff and kinds of skills required to accomplish the scope of work are reflected in the budget justification.

ACF will determine whether the salaries proposed are reasonable, considering salary levels of other similar projects; and, in the case of continuation grants, comparable to those provided in past years. This analysis will also include a review of the time key individuals will spend in relation to their proposed salaries.

If, based on the review, a personnel cost appears to ACF to be unreasonable, then ACF will determine whether the salary rate proposed in the application is consistent with compensation paid under the agency's current pay policy. This might be determined by telephone conversations with the grantee and/or by requesting additional documentation describing established pay scales.

B. Analysis of Employee Fringe Benefits Costs

Fringe benefits are allowable charges to the extent that such benefits are in accordance with the established policy of the grantee organization, required by employer/employee agreement, or required by law.

Fringe benefits may be (a) directly charged by specifically identifying each benefit to each employee; (b) directly charged via a fringe benefit rate; or (c) included in the negotiated indirect cost rate.

An organization is not required to treat all fringe benefits in the same manner. For example, unemployment compensation insurance may be treated as an indirect cost, pension costs may be specifically identified to each employee, and all other benefits may be directly charged via a fringe benefit rate. However, whichever method is used for a given type of fringe benefit must be applied consistently throughout the organization. Regardless of the costing method used, the RDCA will routinely review fringe benefits costs for all organizations with which it negotiates indirect cost rates and will include a substantial amount of information on fringe benefits in the indirect cost negotiation agreement.

ACF determines whether the amount requested is consistent with data in the Indirect Cost Rate Negotiation Agreement, if applicable. ACF also determines whether the correct fringe benefit rate has been used, and that the benefits covered by the rate are not also included as separate costs items in the budget. Similarly, if fringe benefits are specifically identified for each employee, ACF will ensure they are not also included in a collective manner in indirect costs.

If the amount of fringe benefits reflected in the application is not in accordance with information contained in the Indirect Cost Negotiation Agreement, ACF will consult with the RDCA and, if necessary, with the grantee, to assure that the proper amounts in the appropriate categories are charged to the grant.

If the grantee does not have a negotiated Indirect Cost Negotiation Agreement and the amount of fringe benefits appears unreasonable, ACF will compare the types and amounts of fringe benefits proposed with those established by institutional policy to ensure that the grantee organization charges similar types of fringe benefits to other activities, and the policies are reasonable. This information might be obtained through telephone conversation with the applicant or by requesting additional documentation by letter.

C. Analysis of Travel Costs

Travel costs are allowable when the travel will provide direct benefit to the program being supported. Travel costs usually include the cost of transportation, lodging, meals, and incidental expenses incurred by project staff while on official business. Travel and subsistence budget estimates are based on the planned number of trips, places to be visited, length of stay, transportation costs, and subsistence allowances. All travel which does not require per diem is considered local travel.

ACF determines whether the travel costs appear necessary and reasonable in relation to the scope of work for the project.

ACF determines from the application the number of trips anticipated, including the necessity for the number of persons per trip and the frequency of repetitive trips. A review will also be made as to the basis for estimating the travel costs, whether the costs are consistent with institutional travel policies of the applicant organization and whether the grantee's travel policies appear reasonable. If the grantee has no written travel policy of its own, federal travel regulations will be used in determining the amount that may be charged.

If the travel costs appear unreasonable, it may be necessary for ACF to request the grantee organization's travel policy and/or other documentation in a written form.

D. Analysis of Equipment Costs

Equipment is an allowable cost; however, the purchase of equipment must be justified on the basis of need and the unavailability of equipment from other sources within the grantee organization. Purchase of equipment is an "unallowable cost" if the grantee does not have prior written approval from ACF to purchase the item with federal grant funds.

The definition of "equipment" for our purposes is: "tangible nonexpendable personal property, charged directly to the grant award, having a useful life of more than one year and an acquisition cost of $5,000 or more per unit." However, the grantee organization may choose to adopt a lower cost level as its definition of equipment.

ACF determines the need for the equipment, as supported by the narrative portion of the application, i.e., the kind of efforts contemplated to implement the grant program would require the equipment requested.

ACF determines whether the cost for the specific item of equipment appears reasonable, given the cost for such items in similar projects or knowledge of such costs for the class of items requested.

Where appropriate, ACF may ask the grantee to conduct a comparative assessment of the cost advantages of renting or leasing certain types of equipment. This determination should be made on the basis of the length of time the project is expected to be supported and the cost of the rental compared to purchase.

When budgeted expenditures for equipment appear unreasonable, ACF will request the grantee to justify in writing the equipment costs which appear unreasonable.

E. Analysis of Costs for Supplies

Costs for expendable personal property (supplies) are allowable when such supplies are used in the conduct of a grant supported project. To the extent the costs are not excessive or unusual in relation to the overall costs of the project, they do not require specific justification.

ACF determines whether costs for supplies are supported by the narrative description of the project in the application, and appear reasonable in relation to the total amount being requested for the project.

Additional information regarding costs for supplies will be requested if ACF's analysis indicates that budgeted costs may be unreasonable. Details should be provided by the grantee as to types of costs to be incurred and a justification for the amounts requested.

F. Analysis of Request to Purchase Real Property/Facilities -

Federal grant funds may be used to purchase real property (for example Head Start, facilities) if authorized by the applicable federal program statutes/legislation.

The grantee must provide ACF with:

Detailed information demonstrating that the facility purchase will result in savings when compared to alternative facilities which could be leased, purchased or donated, or that there are no such alternative facilities available to the grantee.

A detailed estimate of the cost, if any, of remodeling, renovating or altering the facility to make the facility suitable for a program (i.e., meet licensing standards, fire marshall, disabilities, etc.).

An itemization of all professional fees and related costs associated with and necessary to the purchase of the property. These costs and fees are payable with grant funds, but require prior, written approval from the ACF Regional Office.

An appraisal of the facility by an appropriately certified, independent, disinterested real property appraiser. ACF will determine if there will be any impact from the proposed facility purchase on the grantee's ability to generate non-Federal share, if applicable.

Further details specifically regarding Head Start facilities, and their purchase, construction, alteration and renovation, is in Section G "Analysis of Contract Costs" and in Chapter 12 "Facilities."

G. Analysis of Contract Costs -

Costs for program activities or services procured by the grantee under a contractual arrangement with a third party are allowable.

However, contracts or sub-grants with secondary grantee organizations, including delegate agencies, must be specifically identified, indicating the name and type (i.e., non-profit or governmental entity) of the organization, purpose of contract and estimated dollar amount of the award; and must receive prior written approval from the ACF Regional Office prior to implementation.

Contracts for alterations and renovations and construction of facilities must also be specifically justified, and receive prior written approval.

ACF determines whether the costs for a contract(s) appear to be necessary and reasonable for the conduct of the grant project, and that the costs are supported by the program narrative portion of the application.

If adequate documentation is not provided in the application, justifying awards to secondary grantees (i.e., delegate agencies), or for alternations and renovations, ACF will request such documentation from the grantee.

With respect to alterations and renovations, the justification should clearly establish the following: (a) that the work proposed is consistent with program purposes, and useful life of the building; (b) the alternation and renovation is essential to the project being supported; (c) that the space involved will actually be occupied by the project; and (d) that the work being performed is, in fact, alterations and renovations and not construction.

With respect to construction of facilities, the justification should clearly establish the following: (a) the work proposed is consistent with program purposes and useful life of the facility; (b) the construction is essential to the project being supported; and (c) the facility will actually be occupied by the project.

If the contract is to be awarded for a fixed price based on an estimate of costs, or is a cost type contract, ACF will determine whether the grantee has performed a cost analysis.

In addition, where contract costs (i.e., delegate agency costs) represent a substantial portion of the grant award, ACF will consider whether to perform an independent review of the costs proposed by the subgrantee/delegate agency.

If the costs budgeted for a contract(s) appear unreasonable, ACF will contact the grantee agency and request additional justification for such costs.

H. Analysis of "Other" Costs -

The "Other" category covers all other direct costs not clearly covered in other budget categories. Such costs, where applicable, may include, but are not limited to, insurance, food, medical and dental costs (noncontractual), fees and travel paid directly to individual consultants, printing and publication, computer use, training costs including tuition and stipends, training service costs including wage payments to individuals and supportive service payments, and staff development costs.

All costs included in this category should be clearly delineated, with an explanation of how the costs relate to project activities and objectives. Because space rental and consultant costs are often significant costs proposed in this category, they are discussed in greater detail below:

- **<u>Space Rental Costs:</u>** When facilities are owned by the grantee organization, the costs of these facilities are usually charged through depreciation or use allowances, either directly to ACF supported projects, or included in the indirect cost pool. When an organization leases space, the rental costs are also frequently treated as indirect costs, although they are sometimes treated as direct costs when the space is used only for the grant supported project. In considering space rental costs contained in a grant application, ACF considers whether the costs are necessary for the conduct of the project, and have not also been charged to the project as direct costs (if the same type of costs are included in the indirect cost pool).

    ACF reviews rental costs to assure that the costs are reasonable in relation to the total amount being requested for the project, and consistent with the total period for which project support is contemplated when a lease is used.

    When leases are involved, ACF considers the following factors: rental costs of comparable facilities and market conditions in the area; the type, life expectancy, condition, and value of the facility leased; other facility options available; other provisions of the rental agreement; and the costs of rental space contained in similar proposals for projects in the same community.

    If the amount for space costs appear unreasonable, ACF generally contacts the applicant and requires them to submit written justification for the amount, including the basis on which the costs are computed.

- **<u>Consultants Costs:</u>** Costs for the use of consultants in connection with a grant supported project are allowable. Applicants are encouraged to anticipate their need for consultants and to indicate the proposed use of consultants in their program narrative. There is no need for prior approval for the use of consultants unless the consulting arrangement constitutes a transfer of project activities to a third party (i.e., a delegate agency).

Determination should be made that the use of consultants is necessary for the conduct of the project, and represents a requirement which cannot be met through the use of existing staff resources.

Reasonableness should be weighted in light of such factors as costs for such services in similar projects and the rates for such services in the community, and if appropriate, outside the community.

If the amount for consultant costs appears unreasonable, ACF will generally contact the grantee and a written justification will be requested which would establish the reasonableness of such costs.

CHAPTER 5

OBLIGATIONS AND EXPENDITURES

5.01 PERIOD OF AVAILABILITY OF FUNDS

Grantees may charge to the grant award only allowable costs which result from obligations incurred during the funding period (and any pre-award costs authorized in advance by ACF).

Funds awarded to grantees remain available for obligation at any time during the budget period with the following exceptions:

- Grantees may not obligate grant funds to conduct project activities after grant support ends (meaning after the expiration of the grant funding period, or termination, or denial of refunding of the grant).
- ACF assumes no liability for project costs which exceed the total amount of federal funds authorized on the Financial Assistance Award (FAA). This means that, if a grantee’s obligations exceed the amount of federal funding for that budget period, then the grantee will have to find a non-federal funding source to pay for the excess costs. Grant funds awarded for the following year may not be used to pay for these excess costs.
- Grant funds may not be used for obligations or expenditures made prior to the beginning date of an initial grant for a new project unless pre-agreement costs (also called "pre-award costs") are specifically provided for in the approved budget and have been approved in writing by ACF.
- For grants with "indefinite" project periods, such as Head Start, grant funds remaining at the end of one annual budget period may not be used as "carryover" to pay for obligations incurred during a subsequent budget period unless prior written approval is requested and obtained from ACF.

5.02 WHEN OBLIGATIONS OCCUR

The following table illustrates when an obligation that is directly charged is considered to occur for various kinds of property and services:

If the obligation is for:	The obligation is made:
Services by an employee of the grantee	On the date the services are performed
Services by a contractor	On the date the grantee makes a binding written commitment to obtain the services or work; or On the date the services are received, if there is not an advance written commitment to obtain the services
Accrued vacation	On the date the leave is earned
Public utility services	On the date the grantee receives the services

Travel	On the date the travel is taken
Acquisition of real property	On the date the grantee makes a binding written commitment to acquire the property; or On the date the property is received, if there is not an advance written commitment to obtain the property
Rental of real or personal property	When the grantee uses the property
Acquisition of supplies, equipment, and other personal property	On the date the grantee orders from the vendor; or On the date the grantee makes a binding written commitment for the property
Pre-agreement (i.e., pre-award) costs that were properly approved under the cost principles	On the first day of the effective date of the grant/sub-grant award period

5.03 <u>90-DAY LIQUIDATION PERIOD</u>

All obligations must be incurred by a grantee <u>before</u> the end of the project period, and must be liquidated (i.e., <u>spent</u>) within no more than 90 days after the end of the project period, and reported on the final Financial Status Report (SF-269). For grantees with indefinite project periods (such as Head Start), all obligations must be incurred before the end of the annual <u>budget</u> period, and should be liquidated within no more than 90 days after the end of each budget period. The final SF-269, submitted 90 days after the end of each budget period, should reflect the liquidation of any obligations which remained outstanding at the time the previous report was submitted, and should show as "unobligated balance" any funds the grantee was unable to liquidate timely.

There are times when it is not possible for a grantee to totally liquidate all obligations within the 90-day period. (This situation could occur if, for example, funds were obligated for the purchase of a Head Start bus by ordering it from the dealer, but the vehicle ordered will not be received by the grantee in time to meet the 90-day time frame.) In this situation, grantees may notify ACF in writing and request approval for either a specific extension of time in which to liquidate the obligations, <u>or</u> approval to "carry-over" the funds to the following budget period as additional funds. (In our region, carry-over is generally the method preferred.)

5.04 <u>"CARRY-OVER" AND "OFFSET"</u>

Unobligated balances remaining at the end of a grantee's budget period may be processed by ACF in one of the following ways:

A. By "offsetting" (i.e., deducting) the unobligated balance from the federal share of the approved budget for the <u>current</u> period. For example, $5,000 in unobligated funds from a prior year would be used in place of $5,000 appropriated for the current fiscal year. This will result in no dollar change in the grantee's total federal share of the current budget period.
B. By "carry-over" (i.e., adding) of the unobligated balance to the federal share of the approved budget for the <u>current</u> period. This will increase the grantee's total federal share dollars for the current budget period.

NOTE: Once a "carry-over" is done, federal funds may not be used to offset a deficit if the <u>actual</u> unobligated balance (based on the annual audit) turns out to be less than the amount reported by the grantee on the final Financial Status Report (SF-269). This means that grantees must be very sure of the amount remaining before requesting to carry-over funds to the current budget period. Generally, ACF will request grantees to obtain a certification from their auditor that the funds truly are unobligated, before processing a grantee's request for carry-over. Carry-over of funds to the current budget period is not allowable without prior written approval from ACF.

CHAPTER 6

COST ALLOCATION

6.04 DIRECT COST ALLOCATION PLANS
6.05 INSTRUCTIONS FOR HEAD START GRANTEES
6.06 INDIRECT COSTS
6.07 PROCESS FOR ESTABLISHING INDIRECT COST RATES

6.01 SHARED COSTS

The federal cost principles (OMB Circulars A-21, A-87, and A-122) are designed to provide that the federal government will bear its fair share of costs, except where restricted or prohibited by law. Costs are allocable to a particular grant award in accordance with the relative benefits received. In other words, in order for a cost to be allocable to a grant, the grant program must have benefited in some way from that cost.

Examples of types of shared costs are:

- general administration expenses of the organization, such as salaries and expenses of executive officers, personnel administration, and accounting;
- the costs of operating and maintaining facilities (for buildings shared by more than one program or by administrative staff and program staff), such as utilities, janitorial, rent or depreciation or use allowances; and
- the costs of shared program staff and equipment (for example, a Head Start grantee may also operate a before-and-after-school child care program, using some of the same staff, equipment, and facilities).

6.02 ALLOCATION OF COSTS

A cost is allocable to a federal award if it is treated consistently with other costs incurred for the same purpose in like circumstances, and if it:

- is incurred specifically for the award
- benefits both the award and other work of the organization and can be distributed in reasonable proportion to the benefits received; or
- is necessary to the overall operation of the organization, although a direct relationship to any particular grant cannot be shown.

Any cost allocable to a particular award or other cost objective under these principles may not be shifted to other federal awards to overcome funding deficiencies, or to avoid restrictions imposed by law or by the terms of the award. This means that just because a program receives little funding or doesn't allow for payment of administrative costs, does not mean that program should not still be allocated its fair share of costs. Some programs, such as Community Services Block Grant (CSBG), will agree to pay another program's share of costs, but there must have been an equitable allocation done in order to determine the amount each program should pay. (See Exhibit 6.5 "CSBG-IM-TN-20.")

All costs of the grantee organization, including administrative and indirect costs, must be allocated equitably to each of the various funding sources. Costs may be properly allocated to each funding source using direct cost allocation methods, based on the grantee’s "Direct Cost Allocation Plan," or by using an approved "Indirect Cost Rate Agreement."

6.03 DIRECT COSTS

A "direct cost" is any cost which can be identified specifically with a particular grant award or project, or which can be directly assigned to the project or activity relatively easily with a high degree of accuracy. Costs charged as direct costs to federally-supported projects must be consistently treated as direct costs for other funding sources of the organization.

Some grantees treat all of their costs as direct costs. All of their shared costs, such as depreciation, rental costs, operation and maintenance of facilities, telephone expenses, and the like are prorated individually as direct costs to each category and to each award or other activitiy (using a base most appropriate to the particular cost being prorated). This method is acceptable to use, provided each cost is prorated using a base which accurately measures the benefits provided to each award or other activitiy. The base(s) used must be established in accordance with reasonable criteria, and be supported by current data.

In fact, any method of distribution is acceptable to use so long as it produces an equitable distribution of costs to each funding source.

It is not acceptable to assign a disproportionate share of costs to one program or project simply because it may have the largest funding source.

In theory, all shared costs might be charged as direct costs but, especially for grantees with numerous funding sources and multiple shared cost categories, practical difficulties sometimes prevent grantees using this approach.

6.04 DIRECT COST ALLOCATION PLANS

If the grantee chooses to use direct cost allocation methods, then they must develop a "Direct Cost Allocation Plan." It should use the simplest, most straight-forward ways of allocating costs fairly, to each funding source.

The nature and use of each cost category will determine the appropriate methodology to use for allocation of the cost. For example, costs related to a building that is being shared by several programs could be allocated based on the square footage of building space occupied by each one of the programs. See Exhibit 6.1, titled "Sample Methods for Allocating Shared Costs," for a list of types of shared costs and suggested bases that might be used for direct allocation of each type of cost.

6.05 INSTRUCTIONS FOR HEAD START GRANTEES

ACF's Head Start program has issued 3 different Information Memordandums (IM's) to-date regarding this issue of allocating costs to multiple funding sources, ACF-IM-91-10 [Exhibit 6.2], ACYF-IM-93-18 [Exhibit 6.3], and ACYF-IM-95-27 [Exhibit 6.4].

ACF-IM-91-10, "Head Start Grantees with Multiple Sources of Funding," states:

- Cost allocation methodologies must assign costs proportionally and equitably to all applicable funding sources.
- Any methods of distribution (e.g., time studies or similar analyses based on direct hours of identifiable services provided) may be used which will produce an equitable distribution of cost.
- It is not acceptable to assign a disproportionate share of costs to Head Start simply because Head Start may be the largest funding source.
- Head Start grantees may not loan funds from Head Start to compensate for delayed or late payment from other funding sources.
- Costs allocated to non-Head Start funding sources may not be paid out of the Head Start budget, even on a temporary basis.
- All costs of the organization, including administrative and indirect costs, must be shared equitably by the various funding sources.

ACYF-IM-93-18, "Cost Allocation Plan Requirement for Head Start Programs," states:

- As a general rule, the cost allocation plan should be the simplest, most straight-forward way of allocating costs fairly. Complex, highly detailed plans should be avoided when a simple approach will achieve the objective.
- General schemes that can be applied to large portions of the agency's budget and still fairly allocate costs are preferable to complex detailed schemes.
- Each of the major "cost centers" or cost items in the agency's budget should be looked at for a reasonable, fair way to allocate the costs of that item.

ACYF-IM-95-27, "Reimbursement for Services, Including Medicaid and Child Care, for Head Start Children and Families" states:

- Head Start should be "payer of last resort," when another funding source has primary responsibility for providing a service (e.g., USDA child care food program).
- Carefully document reimbursement arrangements and federal approval.

6.06 <u>INDIRECT COSTS</u>

Indirect costs are the costs incurred by an organization that are not readily identifiable with a particular project or program but are nevertheless necessary to the operation of the organization and the performance of its programs. The costs of operating and maintaining facilities, depreciation, and administrative salaries are types of expenses which are usually treated as indirect costs.

Common examples of indirect costs are:

- General management - president, vice-presidents, executive director, superintendent, etc.
- General organizational expenses - insurance, taxes, legal services, telephone expenses, etc.
- Administrative services - personnel, administration, accounting, procurement, grant/contract administration, business office, etc.
- Operation and maintenance of facilities - utilities, janitorial services, repairs, etc.
- Depreciation or use allowances on buildings and equipment.
- Fringe benefits applicable to administrative staff, and, occasionally, fringe benefits applicable to project staff.

In theory, all of these costs might be charged directly; however, practical difficulties frequently preclude this approach. Therefore, these costs are normally grouped into a common pool(s) and distributed to benefiting organizational activities through a cost allocation process. The end product of this allocation process is an indirect cost percentage rate (or rates) which is then applied to individual grant awards to determine the amount of indirect costs chargeable to each of the awards. The rate(s) represents the ratio of indirect costs to a direct cost base (commonly direct salaries and wages) and is expressed as a percentage of the base, e.g., 20% of direct salaries and wages.

An indirect cost rate agreement is established on the basis of an indirect cost proposal submitted by grantees to the HHS/Regional Division of Cost Allocation (RDCA). (If the grantee is under the indirect cost negotiation cognizance of a Federal agency other than HHS, its indirect cost proposals should be submitted to that agency.)

Indirect costs are reimbursed to an organization based on its established rate, subject to administrative and legislative limitations, as part of the costs of individual grants. It is ACF policy to fully fund an approved applicant's requested indirect costs, if such costs are determined to be allowable and consistent with the applicant's Indirect Cost Negotiation Agreement. Some programs, such as Head Start, have limits on the total amount of administrative costs that may be charged, which could preclude payment of all indirect costs if the rate is very high. In that situation, grantees must try to find another funding source willing to pay the excess costs, or find a way to reduce the amount of their overall administrative costs.

6.07 <u>PROCESS FOR ESTABLISHING INDIRECT COST RATES</u>

A. <u>Submission of Proposals</u>

An organization that has <u>not</u> previously established an approved indirect cost rate must submit an initial indirect cost proposal to the RDCA, and submit a copy to the ACF Regional Grants Officer, immediately after being notified that a grant providing for the reimbursement of indirect costs will be awarded by ACF. Where possible, this proposal should be submitted to the RDCA prior to the date the grant is awarded, but no later than three months after the effective date of the grant. Non-profit grantee organizations should review "A Guide for Non-Profit Organizations" [Exhibit 6.6] for further information on preparing and submitting a proposal for an indirect cost rate.

The proposal, which will be used to establish a rate to permit funding of indirect costs under the award, should normally be based on the organization's actual costs for its most recently completed fiscal year. However, if the organization is aware of factors that are expected to result in a significant change in the rate for the fiscal year during which the grant is to be performed, the proposal must also consider projected costs of that year.

Organizations that <u>have</u> previously established indirect cost rates must submit a new indirect cost proposal to the RDCA within six months after the close of every fiscal year. The type of rate(s) reflected in the proposal and the fiscal year(s) on which the rate should be based will be governed by the specific circumstance involved for each grantee agency.

The organization's initial proposal as well as each succeeding annual proposal must be accompanied by, and be cross-referenced and reconciled to, its independently audited financial statements (which account for all activities for the fiscal year on which the proposal is based). If independently audited statements are not available, the grantees should contact the RDCA to determine what other financial documents will be acceptable to substantiate the amounts reflected in the proposal. If a rate in the proposal is based on projected costs for a future fiscal year, the rate computation must be cross-referenced and reconciled to the organization's budget for the year. In these cases, the future fiscal year's budget <u>and</u> the financial statements for the most recently completed fiscal year must be submitted with the proposal.

B. <u>Regional Division of Cost Allocation</u>

The RDCA will review the indirect cost proposal(s) submitted by grantee organizations, and, based on these reviews, will negotiate appropriate indirect cost rates with the grantees. If an audit is deemed necessary, the RDCA will request the audit from the OIG Office of Audit or will request ACF review to ensure there is no duplication of costs.

The address for the RDCA for our region is: Regional Division of Cost Allocation, 1301 Young Street, Room 732, Dallas TX 75202. Their telephone number is: (214) 767-3600.

C. <u>Indirect Cost Negotiation Agreement</u>

The results of each negotiation will be formalized in an Indirect Cost Negotiation Agreement signed by the appropriate RDCA official and an authorized representative of the grantee.

Each agreement will include the following provisions:

- The agreed upon rate(s) and information directly related to the use of the rate(s) (e.g., type of rate, effective period, direct cost base, etc.).
- The treatment of fringe benefits as either direct or indirect costs.
- General terms and conditions of the agreement.
- Special terms and conditions of the agreement, if any (e.g., the direct charging of a type of cost that is normally treated as indirect by other grantees).

D. <u>Disputes</u>

Disputes arising in the negotiation of indirect costs rates will be resolved at the HHS regional office level in accordance with the informal appeals procedures described in the Department's indirect cost appeals regulations (45 CFR Part 75). Disputes that cannot be resolved at the HHS regional office level will be resolved in accordance with the procedure contained in the Department's grant appeals regulations (45 CFR Part 16).

CHAPTER 7

NON-FEDERAL SHARE

7.01 <u>GENERAL INFORMATION</u>

Whatever name you call it by, "non-federal share," "in-kind," or "matching," federal grant programs require that the grantee must also contribute a portion of the total cost of the project.

For example, Head Start requires a minimum non-federal share of 20 percent of the total costs of the program (45 CFR Part 1301.20); and the Runaway and Homeless Youth Act requires that the grantee must provide a non-federal match that equals at least 10 percent of the federal funds that will be received (45 CFR Part 1351.13). The specific percentages of maximum federal financial participation may be found in the applicable program regulations, legislation and/or the program announcement for each grant.

Match expenditures may be in the form of cash or they may be "in-kind" contributions of goods or services (such as donations of needed equipment or volunteer services in the program).

ACF enforces grantee matching requirements on a project period (as opposed to budget period) basis for all discretionary awards, other than Head Start awards which have indefinite project periods. Grantees (such as Early Head Start for example) may provide the required non-Federal share at any time during the project period, not necessarily in proportionate amounts annually. Since Head Start grants have indefinite project periods, grantees are required to provide matching or cost-sharing annually, on a budget period basis.

7.02 REQUIREMENTS FOR NON-FEDERAL SHARE

Grant applications must include proposed budgets for both the federal funds and the non-federal matching funds. Then the Financial Assistance Award (FAA) document will constitute written approval of both the federal and non-federal budgets as described in the grantee's application.

As stated in federal regulations, 45 CFR 74.23 and 92.24, in order to be accepted, all cost sharing or matching contributions, including cash and in-kind, must meet all of the following criteria:

- Are verifiable costs from the grantee's accounting records.
- Are not already included as match contributions for another federally-assisted program.
- Are necessary and reasonable costs for proper and efficient accomplishment of the grant program's objectives (for example, the services provided by the volunteer would have to be otherwise purchased or provided by salaried personnel)
- Are allowable costs under the applicable federal cost principles (OMB Circulars A-21, A-87, and A-122), and so federal funds could have been used.
- Are not paid by the federal government under another award, unless specifically authorized by federal statute to be used for cost sharing or matching.
- Are provided for in the approved budget.

7.03 CASH MATCH AND "IN-KIND" DONATIONS

- "Cash match" can be from State funds, local funds, private or corporate donations, program income (if prior approval is received to count as match), or any other non-federal funds. The grant application must identify both the source and the proposed use for cash match.

    NOTE: Cash donations do not count as match until the date the cash is actually spent for a program purpose cost, not on the date when the cash was received.

- "In-kind donations" could be in the form of volunteer services to the program; loaned equipment or space; donated supplies; or donated land, buildings, or equipment.

    To be allowable, in-kind donations must be costs that could have been paid with federal grant funds, had they not been donated to the program. This means that donations of items or services outside the scope of the grant, could not be counted as in-kind match for that grant. For example, donations of food to help re-stock an organization's community food bank could not be counted as an in-kind match for the Head Start program (not even for the food taken home by Head Start families), because it is outside the scope of that grant purpose.

7.04 VALUATION OF "IN-KIND" CONTRIBUTIONS

As stated in 45 CFR 74.23 and 92.24, values for in-kind contributions of services and property must be established in accordance with the regulations and the appropriate federal cost principles:

- Value of donated land and buildings will be its fair market value at the time of the donation, as established by an independent appraiser (certified, real property appraiser);
- Value of donated equipment will be the fair market value of equipment of the same age and condition at the time of the donation;
- Value of donated space within a building (or playground, parking lot, etc.) will be the fair rental value of comparable space, as established by an independent appraisal of comparable space and facilities in a privately-owned building in the same area;
- Value of loaned equipment will be its fair rental value; and
- Value of volunteer services will include salary and fringe benefits rates, and will be consistent with amounts paid for similar work in the grantee's organization. (If the required skills are not found in the grantee's organization, then the value will be consistent with salary plus fringe benefits paid for similar work in the local labor market.)

7.05 SUPPORTING DOCUMENTATION

Federal regulations state that volunteer services must be documented and, to the extent feasible, supported by the same methods used by the grantee for its own employees, including time records. Documentation should include signatures of volunteers certifying the day of service, hours and rate of pay, and state the service performed. The form should be validated by a responsible grantee official.

The value of donated space must be documented by an independent appraisal of comparable space and facilities in a privately-owned building in the same locality.

The regulations also state that the basis for determining the valuation for personal service, material, equipment, buildings and land must be documented.

7.06 ACF/GRANTS ADMINISTRATION MANUAL

At the end of this chapter is a copy of Section 3.05 "Matching or Cost Sharing" from the ACF/Grants Administration Manual (GAM). [Exhibit 7.1] Although the GAM is an internal document written primarily to address federal staff processes, this particular section contains information directly applicable to ACF grantees.

In Section 3.05.407 for example, is information regarding valuation of volunteer services, and examples of various types of volunteer services. Use of other federal funds as match, is found in Section 3.05.408. How to figure the computation of match for a grant is found in Section 3.05.409.

CHAPTER 8

ADMINISTRATIVE COSTS

8.01 "ADMINISTRATIVE COSTS" AND "DUAL BENEFIT COSTS"

"Administrative costs" are those costs related to organization-wide management functions plus the costs of management functions for each individual program within the organization. These costs can be in both the personnel and non-personnel categories.

All grantees <u>must</u> identify and charge the costs of all management functions as administrative costs. These functions include planning, coordination and direction; budgeting, accounting, and auditing; and management of payroll, personnel, purchasing, and property.

In order to identify all administrative costs it is generally necessary for grantees to have a code (or codes) in their accounting Chart of Accounts which identifies these costs as administrative costs.

"Dual benefit costs" are costs that are associated with both the delivery of program component services <u>and</u> administrative functions. In such cases, grantees must identify and allocate appropriately the portion of the costs that are for administration and the portion that are program costs.

For example, a Head Start Director might need to fill-in one day for an absent teacher. The Head Start Director's salary for that pay period would then be allocated partly as a program cost (for the time spent providing direct services in the classroom) and partly as an administrative cost (for the time spent directing the program).

When administrative staff and program staff occupy space in the same building, space costs, and costs related to space, such as utilities, are dual benefit costs. The grantee must determine and allocate the amount or percentage of space dedicated to administration and the amount for program functions, in order to charge the costs appropriately.

8.02 <u>LIMITATIONS ON ADMINISTRATIVE COSTS</u>

Some ACF programs, such as Head Start, set limits on the maximum amount of administrative cost that may be incurred. Allowable administration cost for Head Start grantees may not exceed 15 percent of the total annual approved costs of the program, unless a temporary waiver was granted by ACF. (See Exhibits 8.1 and 8.2.) This limit of 15 percent for administrative costs is a maximum. In cases where the administrative costs are at or even below 15 percent, but are judged by ACF to be excessive, the grantee must eliminate the excessive administrative costs.

As stated above, in Section 8.01, grantees need codes within their accounting records in order to identify administrative costs. This will enable grantees to maintain a running tally of the total administrative costs charged to-date to each program (for program-specific administrative costs plus each program's share of organization-wide administrative costs). It is also a good idea for grantees to include administrative costs as a column on their monthly budget comparison reports provided to program managers (so they can ensure administrative cost limits will not be exceeded).

8.03 <u>TYPES OF ADMINISTRATIVE COSTS</u>

Administrative costs include, but are not limited to, the salaries of the executive director, personnel officer, fiscal officer, bookkeeper, purchasing officer, payroll/insurance/ property clerk, janitor for administrative office space, and costs associated with volunteers carrying out administrative functions.

Administrative costs also include expenses related to administrative staff functions such as the costs of fringe benefits, travel, per diem, transportation, and training for administrative staff.

Other administrative costs are expenses related to bookkeeping and payroll services, audits, and bonding; and, to the extent they support administrative functions and activities, the costs of insurance, supplies, copy machines, postage, utilities, and occupying, operating, and maintaining space.

8.04 <u>ADMINISTRATIVE COSTS AND INDIRECT COSTS</u>

Costs categorized as administrative costs are frequently charged to the grant as indirect costs, because these costs are so often shared costs. But this does <u>not</u> mean that administrative costs and indirect costs are the same.

<u>Some</u> administrative costs, such as the salary of a program director, will be charged 100% to a single funding source as a direct charge, and <u>some</u> indirect cost pools will include shared <u>program</u> costs, such as happens often with Child Care and Head Start.

Organization-wide administrative costs will need to be allocated to each benefiting funding source, and will be a part of the grantee's total indirect cost computations.

Administrative costs that are not organization-wide, such as the salaries and related expenses of program directors, and bookkeepers assigned work for only one program, will not be part of the indirect cost computation. (See Chapter 6 "Cost Allocation" for more information on cost allocation and indirect cost rates.)

CHAPTER 9

PRIOR APPROVALS

9.01 WHEN PRIOR APPROVAL IS REQUIRED

1. In accordance with federal regulations in 45 CFR 74.25 and 92.30, grantees must obtain prior approval, in writing, from the ACF Regional Office whenever any of the following changes is anticipated:
2. Change of the "scope" or objective of the program (such as changing from center-based to home-based Head Start), even if there is no associated budget revision requiring prior written approval.
3. Change of the program director or other key persons specified in the grantee's application or on the award document (i.e., the FAA - Block 15).
4. The absence for more than three months, or a 25 percent reduction in time devoted to the program, by the approved program director.
5. The need for additional Federal funding.
6. The inclusion, unless waived by the HHS awarding agency, of costs that require prior approval in accordance with the applicable federal cost principles (OMB Circulars A - 122, A - 87, or A-21), such as purchase of equipment with a per unit cost of $5,000 or more.
7. The transfer of funds allotted for training allowances (in Head Start, for example, this would be the CAN 4120 funds) to other categories of expense.
8. The carry-forward of unobligated and/or unliquidated balances of federal funds from one funding period to a subsequent funding period.
9. Unless described in the application and funded in the approved award, the sub-award, transfer, or contracting out of any work under an award; such as the use of Head Start delegate agencies. (This provision does not apply to vendor contracts for the purchase of supplies, material, equipment, or general support services.)
   Grantees must also obtain written, prior approval from the ACF Regional Office for the following (based on federal regulations and/or cost principles):
10. Before purchasing, constructing and/or making major renovation to facilities.
11. Before making any fund or budget transfers between construction and non-construction line items.
12. Before incurring costs for foreign travel.
13. Before the use of sole source vendor contracts.
14. Before the use of indirect cost rates.
15. To obtain a temporary waiver of non-federal share matching requirements.
16. To obtain a temporary waiver of administrative cost limitation requirements.
17. Before the purchase of an item of equipment costing over $5,000.

9.02 REQUESTING AND RECEIVING PRIOR APPROVAL

All grantee requests that require prior approval must be submitted in writing to the ACF Regional Grants Officer. The grantee will receive written notification of approval/disapproval through either a Financial Assistance Award (FAA) or a letter.

As provided in 45 CFR Parts 74.25 and 92.30, approvals are not valid unless they are in writing and signed by an authorized official. In this region, all prior approvals must be signed by either the ACF Regional Grants Officer or the responsible Program Official or the Regional Administrator Director.

9.03 RETROACTIVE APPROVAL

In exceptional cases, grantees who failed to obtain a required prior approval may submit a request for retroactive approval. However, such approvals shall be granted sparingly and only if:

- The transaction would have been approved had the approval been requested in advance; and
- The grantee agrees to institute controls to ensure that prior approval requirements are met in the future.

9.04 DELEGATES AND SUB-GRANTEES

Grantees shall be responsible for reviewing requests from their sub-grantee/delegate agencies, for the approval required. If an action by a sub-grantee/delegate will result in a change in the overall grant project or budget requiring ACF approval, the grantee must obtain that approval (from ACF) before giving its own approval to the sub-grantee/delegate. Approvals shall not be valid unless they are in writing and signed by an authorized official of the grantee.

9.05 BUDGET CHANGES

The approval of a grantee budget constitutes prior approval for the expenditure of funds for the specific items included in that budget. Except as provided below, grantees may make revisions between and among the object class categories within the total approved budget of the project, provided funds are used for allowable costs of the project. (No transfers may be made which would cause the funds to be used for purposes other than those intended, or which adversely affect or significantly change the grant/sub-grant approved project.)

All requests for budget changes that require prior approval should be submitted to ACF at least 45 days prior to the requested effective date of the change. Simple line item changes will not require formal budget revision by ACF and will not require ACF approval. (For example, to move $15,000 from "Other" to "Supplies.")

The cost principles prescribed in 45 CFR Part 74.27 and 45 CFR Part 92.22 state that before certain types of costs are incurred, prior approval must be obtained. The cost items requiring prior approval differ somewhat among the various cost principles; consequently, different types of grantee and sub-grantee organizations are subject to different requirements.

9.06 PROGRAMMATIC CHANGES

A. SCOPE.

The grantee shall obtain prior approval for any change to the scope or objectives of the approved project. Changing the scope or objectives may result from a significant alteration of the approved project activities, change in the direction of the project, the types of services delivered, the number of beneficiaries to be served, or training provided.

Upon receipt of a grantee request to change its scope of work, ACF will closely review the request to determine if the proposed changes would significantly expand or otherwise alter the scope and purpose of the grant as originally awarded.

B. KEY PERSONNEL.

The grantee shall obtain prior approval of the following anticipated changes in key personnel:

- To continue the project for more than three months without the active direction of an approved project director. The grant may be terminated if the arrangements made by the grantee are not approved by ACF.

- To permit the project director (or any other persons named and expressly identified as key project people in the notice of grant or sub-grant award) to devote 25 percent less time to the project than was anticipated when the grant or sub-grant was awarded.
- To replace the project director (or any other persons named and expressly identified as key project people in the grant/sub-grant award document).

C. SUB-GRANTEES/DELEGATES

The grantee must obtain prior approval if it plans to provide financial assistance to another party by sub-granting or any other means.

The grantee must obtain prior approval before transferring to others (by contracting, sub-granting, or any other means) any work under the grant award, unless described in the application and funded in the approved award. This provision does not apply to the procurement of supplies, materials, equipment or general support services.

A grantee may not act merely as a straw-party (i.e., to act as a mere conduit of funds to another party without performing a substantive role itself). Therefore, ACF shall authorize a grantee to transfer programmatic work only if the grantee will perform at least one of the following roles:

- Principal performer of project activities;
- Primary beneficiary of Federal financial assistance; or
- Overall administrator of a program in which other parties perform activities or receive financial assistance

CHAPTER 10

PROCUREMENT

10.01 PROCUREMENT STANDARDS
10.02 PRICE/COST ANALYSIS
10.03 COMPETITION
10.04 CODE OF CONDUCT
10.05 DOCUMENTATION

10.01 PROCUREMENT STANDARDS

The federal regulations, in 45 CFR 74.40 through 74.48 and 45 CFR 92.36, set standards for use by grantees in establishing their own procedures for purchasing services, supplies and other expendable property, equipment, and real property with federal funds. These standards are established to ensure that grantees obtain materials and services with federal funds in an effective manner and in compliance with federal laws.

Based on the regulations in 45 CFR 74.44 and 92.36, all grantees must establish and follow written procurement procedures for making purchases with federal funds. Grantees that are State governments will follow the same written policies and procedures they use for procurements from non-federal funds.

1. Grantees that are local governments, tribal governments, non-profit organizations, or universities will ensure that their written procurement procedures provide, at a minimum, that:
2. Grantees will take steps to make economical purchases and avoid purchasing unnecessary or duplicative items. (This means, of course, that grantees must have some sort of mechanism for determining what items they already have, such as an inventory system.)
3. Grantees will analyze (prior to doing either one) whether leasing or purchasing an item is the most economical and practical alternative, in the long run, for the grantee and for the federal government. Leasing should be used in lieu of purchasing when it is the more economical and practical alternative. This requirement essentially directs grantees to buy only what they need and purchase items in the most economical way.
4. Grantees will provide solicitation advertisements for goods and services that contain all of the requirements of 45 CFR 74.44 or 92.36, as required.

5. Grantees will make positive efforts to utilize small businesses, minority-owned firms, and women's business enterprises, whenever possible, and must take all of the steps required by 45 CFR 74.44 or 92.36, as required.
6. Grantees will maintain written standards of conduct governing staff who are involved in the award or administration of contracts, including vendor contracts, lease contracts, and program or administrative services contracts. (See Chapter 11 "Contracts and Leases" for more information.)

   Grantees will conduct all procurement transactions in a way that provides for open and free competition. (See Section 10.03 below.)

7. Grantees will make some form of cost or price analysis, and document it in the files, for every procurement action. (See Section 10.02 below.)
8. Grantees will maintain procurement records and files for purchases, as required. (See Section 10.05 below.)
9. Grantees will maintain a system for contract administration, including vendor contracts, lease contracts, and program or administrative services contracts. The system should also include procedures regarding settlement and satisfaction of contractual disputes or other matters of a contractual nature. (See Chapter 11 "Contracts and Leases.")

10.02 PRICE/COST ANALYSIS

Federal regulations require that some form of cost or price analysis must be made and documented in the procurement files in connection with every procurement action using federal grant funds. This means that grantees are required to analyze costs to determine if the amount seems reasonable.

There are various ways to conduct a "price analysis." These include comparing offered prices with those listed in commercial catalogs, or with those recently submitted for similar services. It can be done, for example, by comparing price quotes submitted by vendors, or simply by comparing published market prices (such as supply catalog prices, for example).

While price analysis involves a comparison of marketplace prices, "cost analysis" involves an examination of all the elements used in calculating a contract's total estimated cost. When fixed-price contracts are based on cost estimates, grantees should perform a cost analysis to determine the reasonableness of cost or price. Cost analysis is the review and evaluation of each element of cost to determine whether it is reasonable, allocable to that grant program, and an allowable cost for that grant program. Every cost element listed in the vendor's offer must be examined. Through a cost analysis , determinations are made on which costs are real and reasonable, allowable under grantee regulations or rules, and properly allocated to the work to be performed under the proposed contract. A cost analysis is also required when contract modifications introduce new conditions, that were not examined under the previous analysis, or where more current information is needed.

10.03 COMPETITION

All procurement transactions, regardless of amount, must be conducted in a manner that provides, to the maximum extent practical, open and free competition. This means that, even if it seems like a "good deal," grantees cannot make the purchase until other vendors are also given consideration.

In order to eliminate unfair advantage, contractors that develop or draft grantee applications or contract specifications or requirements (or statements of work, invitations for bids and/or requests for proposals) must be excluded from the competition for that procurement.

Solicitations should clearly state all the requirements the vendor must fulfill in order for the bid or offer to be evaluated by the grantee.

The procurement should be given to the vendor whose bid or offer is responsive to the solicitation, and is most advantageous to the grantee (considering price, quality, and other factors).

Most ACF grantees use an annual bidding system for procuring items in bulk such as classroom supplies, office supplies, paper products, cleaning supplies, etc.; and for procuring program and administrative services to be provided by outside contractors. Once a vendor has been selected, that same vendor is then used all year. This enables the grantees to get better prices, and saves staff time.

School districts and other local government agencies, and even some of our community action agencies, are sometimes allowed to buy from their State's vendors list, so the competition process has already been done. Governmental grantees are also encouraged to use inter-governmental agreements for purchasing, to use cooperative purchasing, and consortium arrangements. When feasible, governmental grantees are also encouraged to use federal excess and surplus property in lieu of purchasing new items.

Most grantees also establish, as part of their written procedures, a "tiered" system regarding which staff member is authorized to approve procurement at various price levels, and what competition method is to be used at various price levels. For example, for items under $500 local center directors might be authorized to approve the purchase and pay for it out of their petty cash fund. Procurements between $500 and $1,000 might need program director approval and be purchased using telephone quotes from vendors or comparison of catalog prices. Procurements between $1,000 and $5,000 might need approval of the executive director and need written quotes from at least three vendors. Procurements over $5,000 (and audits and other annual bid items) might need board approval and require formal advertising with sealed bids. The actual written procedures and policies would be more involved, of course, than what is listed here, and each grantee organization must decide what they feel comfortable establishing at each level (in consultation generally with their insurance provider and their auditor).

10.04 CODE OF CONDUCT

Grantees must maintain written standards of conduct governing the performance of employees who are involved in the awarding or administering of contracts. This generally includes, at a minimum, the procurement officer, contract administration officer, and grantee officials who sign or authorize contracts. Further information on this is in Chapter 11 "Contracts and Leases."

10.05 DOCUMENTATION

As stated in Section 10.02, price analysis and cost analysis for each procurement transaction must be documented in the procurement files.

For price analysis, this means keeping copies of all the documentation of what prices and vendors were compared, identifying which vendor was chosen, and stating why that vendor was chosen. Most grantees use a form for each procurement transaction, with columns for each vendor and price. At the bottom of the form is space for a narrative statement of which vendor was chosen and why. The form is then signed and dated by the procurement officer, and signed/approved by the appropriate authorizing official. All supporting documents are stapled to the back of the form, and the form is filed in the vendor file of whichever vendor was chosen. It is not a requirement that all grantees use this exact process, but a variation of this process is used by most of our grantees.

For cost analysis, this means keeping written documentation of the determination of whether a cost was reasonable, allocable to that grant, and allowable for that grant. Most grantees assign the program directors the task of determining whether an anticipated procurement would be an allowable cost for their grant program, and the program director's signature (generally on the purchase requisition) is used to authorize charging that cost to their program. If a cost is an allocated cost, such as long distance charges on a telephone bill, each of the program directors could be asked to identify the charges for their grant program, and sign to authorize charging the costs to their program. These forms are also generally maintained in the appropriate vendor files.

In addition, all purchase orders should be maintained in the vendor files (after the items are received). All purchase requisitions should be stapled to the purchase orders (after they are approved and ordered). Pending requisitions and pending purchase orders should be maintained in a file and monitored regularly. Vendors should be paid from original invoices, and most of our grantees use multi-copy checks so that the invoice and one check copy can then be placed in the vendor files.

For procurement transactions involving advertisement and a formal bid process, all of the documents prepared during the entire cycle should be maintained, and again the easiest and best place to keep it is in the vendor file of whichever vendor is selected. (Prior to selection of a vendor, the documents are generally kept in a file by the procurement officer.)

CHAPTER 11

CONTRACTS AND LEASES

11.01 GENERAL INFORMATION

The term "contracts" as used here includes vendor contracts for purchases, service provider contracts, construction contracts, lease agreements (for buildings, space, vehicles, office equipment, etc.), and any other legally binding commitments for purchasing or leasing that a grantee may sign.

Based on federal regulations, contracts should be made only with responsible contractors who possess the potential ability to perform successfully under the terms and conditions of the proposed procurement. The regulations also state that, in making the selection, consideration should be given to such matters as contractor integrity, record of past performance, financial and technical resources or accessibility to other necessary resources. Note that this means the lowest bid for a contract will not always be the vendor selected.

11.02 GRANTEE RESPONSIBILITY

The federal procurement and contracting standards do not relieve grantees of their contractual responsibilities arising under their contracts. The grantee is the responsible authority, without recourse to the federal government or any ACF staff member, regarding the settlement and satisfaction of all contractual and administrative issues arising out of procurements entered into in support of a grant award. This includes disputes, claims, protests of award, source evaluation or other matters of a contractual nature.

What this means is that grantees are responsible for whatever contractual agreements their officials sign, not the federal government. For example, if a grantee agency signs a long-term contract agreement that does not have a clause allowing for termination, then the grantee must honor that contract for however long it lasts, even though they may have lost their federal funding, or found a better deal, or whatever.

11.03 CONTRACT ADMINISTRATION

Grantees are required to maintain a system of contract administration to ensure contractor conformance with the terms, conditions, and specifications of the contract. In fact, grantees are required to evaluate their contractors' performance, and to document whether or not each contractor has met the terms and conditions of the contract. Grantees with large staffs and/or with large numbers of contracts, usually have a contract officer, whose job it is to monitor contractors, document their performance, and make recommendations concerning contract renewals, and even continued payment of a contractor. Smaller grantees and ones with fewer contracts, may have this function as a part of the applicable program director's job.

In addition, grantees are required to ensure adequate and timely follow-up of the delivery of all purchases ordered from vendors. For example, grantees should follow-up on items vendors have indicated as "back-ordered" to determine when the items will be received. After a period of time, it might be necessary to cancel an order, and re-order from another vendor. The vendor's inability to provide the items in a timely manner should be documented and considered when procuring like items in the future.

11.04 CONTRACT PROVISIONS

Grantees should include, in addition to provisions to define a sound and complete agreement, the following provisions in their contracts and sub-contracts:

- Provisions that allow for administrative, contractual, or legal remedies in instances in which a contractor violates or breaches the contract terms, and provide for appropriate remedial actions.
- Provisions for termination by the grantee, including the manner by which termination shall be effected and the basis for the settlement; and conditions under which the contract may be terminated for default; as well as conditions where the contract may be terminated because of circumstances beyond the control of the contractor.
- Contracts for construction or major renovations should contain provisions relating to bid guarantees, performance bonds, and payment bonds, as required.

In addition, all contracts awarded by a grantee, including small purchases, should contain the required provisions listed in 45 CFR Part 74, Appendix A, "Contract Provisions," <u>when appropriate</u>, such as the Copeland Anti-Kickback Act provisions, the Davis-Bacon Act provisions, the Contract Work Hours and Safety Standards Act provisions, etc.

11.05 <u>CODE OF CONDUCT</u>

Grantees must maintain a written code of standards of conduct governing the performance of their employees who are involved in the award, authorization, and administration of contracts with vendors, service providers, and lease holders. The requirements for this are found in 45 CFR 74.42 and 92.36(b)(3).

The written standards must state that no grantee employee, officer, or agent will participate in the selection, award, or administration of any contract supported by federal funds, if a real conflict of interest would be involved, or even if an appearance of a conflict of interest or a potential conflict of interest would be involved. The regulations state that:

> "Such a conflict would arise when the employee, officer, or agent, or any member of his or her family, or his or her partner, or an organization which employs or is about to employ any of the parties indicated herein, has a financial or other interest in the firm selected for an award."

In addition, the written standards of conduct must state that no grantee employee, officer, or agent (or any member of his or her family, or his or her partner, or an organization which employs or is about to employ any of the parties indicated herein) will solicit or accept money, gifts, favors, or anything of monetary value, from contractors or parties to sub-agreements. However, grantees may set standards for situations in which the financial interest is not substantial or the gift is an unsolicited item of nominal value.

The written standards must also include provisions for disciplinary actions to be applied for violations of such standards by its employees, officers, or agents. Most grantees make this code of conduct a part of their personnel manual and/or have employees sign a written statement that they will not violate these standards, and acknowledging that such a violation is automatic grounds for immediate disciplinary action (i.e., firing, demotion, leave without pay, etc.).

In addition, Head Start's own program regulations, in 45 CFR 1304.52(g)(2)&(3), state that: "(2) Grantee and delegate agencies <u>must</u> ensure that all employees engaged in the award and administration of contracts or <u>other</u> financial awards sign statements that they will not solicit or accept personal gratuities, favors, or anything of significant monetary value from contractors or potential contractors. (3) Personnel policies and procedures must include provision for appropriate penalties for violating the standards of conduct."

11.06 <u>LEASES</u>

Since leases are a form of contract, all of the above contracting rules also apply to the award and administration of lease agreements, whether the lease is for a building, classroom space, vehicle, or office equipment, etc.

CHAPTER 12

FACILITIES

12.04 DAVIS-BACON ACT
12.05 FACILITY REFERRAL AND INFORMATION SERVICE (FRIS)

12.01 GENERAL INFORMATION

Of ACF discretionary grant programs, only Head Start currently has authority to use federal grant funds to purchase or construct facilities. Therefore, this chapter applies only to Head Start and Early Head Start grantees.

Final federal regulations, in 45 CFR 1309, were published in the Federal Register on February 8, 1999 for the purchase of Head Start facilities. In the same Federal Register, an NPRM (Notice of Proposed Rulemaking) was also published for the construction or major renovation of Head Start facilities. Head Start then issued ACYF-IM-HS-99-01 on February 12, 1999 which included an explanation of the regulations [Exhibit 12.1].

Grant awards authorizing the purchase of facilities also require grantees to record a Notice of Federal Interest in the facility in the appropriate local government records.

Federal regulations in 45 CFR 1309.22(a) have been revised to include provisions required in a mortgage agreement, signed by a grantee borrowing money to finance the purchase of a facility, regarding circumstances in which the grantee defaults on the loan or ceases to be the designated Head Start agency. For example, the mortgage agreement must provide that, in the case of a default by the grantee, ACF has the right to ensure the default is cured by the grantee or another agency designated by ACF.

The regulations were also revised to state that grantees must provide physical destruction insurance for the full replacement value of the facility.

Facilities acquired with ACF grant funds, in full or in part, must be used for the purposes consistent with the grant award and in the manner for which it was awarded. The facility must be used for the purpose originally authorized as long as it is needed for that purpose. Prior approval must be obtained from ACF to use the property for any other purpose.

Facilities acquired with ACF grant funds may not be transferred, assigned, mortgaged, used as collateral, leased, or in any manner encumbered by the grantee unless specifically authorized in writing by ACF.

All records pertinent to the purchase and debt must be retained by the grantee for a period equal to the life of the federal interest in the property plus 3 years.

Certified copies of the deed, loan instrument, mortgage, and any other legal documents related to the purchase of the real property, or to the discharge of any debt secured by the real property, must be submitted to the ACF Regional Grants Officer within 10 days of their execution.

Any audit of a grantee, which has acquired (through purchase or construction) or made major renovations to a facility with grant funds, shall include an audit of any mortgage or encumbrance on the facility.

12.02 APPLICATION REQUIREMENTS - PURCHASE

ACF/Region VI has created a "Facility Application Requirements Checklist" [Exhibit 12.2] to try to make it easier for grantees to put together a complete application package. The 45 CFR 1309 Head Start regulations require grant applications for purchasing facilities to include the following information:

A. A legal description of the site of the facility proposed to be purchased, including:

1) An explanation of the appropriateness of the location to the grantee's service area;

2) A statement of the effect that the purchase of the facility will have on the transportation of children to the program;

3) Grantee's ability to collaborate with other child care, social services and health providers, and on all other program activities and services.

B. Plans and specifications of such facility, including:

1) Information on the size and type of structure;

2) The number and description of rooms;

3) The lot on which the building is located, including space available for a playground and parking area.

C. A comparison of the cost of the proposed facility to the cost of the facility currently used by the grantee, unless the grantee:

1) Has no current facility;

2) Will lose the use of the current facility;

3) The grantee intends to continue to use its current facility; or

4) Has shown to the satisfaction of the responsible HHS official that the existing facility is inadequate.

In cases noted in 1-4 above, a comparison of the cost of the proposed facility to the cost of another facility comparable in size to the facility proposed to be purchased, suitable for use as a Head Start facility (or which can be made suitable through renovation, the cost of which shall be included in the cost comparison) and which is available for rent in the service area.

All costs of purchase and ownership must be identified as one-time costs or ongoing costs.

The period of comparison is twenty years for non-modular facilities and ten years for modular/portable facilities.

D. A detailed description of renovations, plans and specifications for the facility after renovations are complete. Include a certification by a licensed engineer as to the cost and technical appropriateness of the proposed renovations.

E. State the intended use of the facility including:

1) Information demonstrating that the facility will be used as a Head Start Center, or a direct support facility for Head Start.

2) For additional uses, other than for Head Start, state what portion of the facility is to be used for other purposes, state the purpose, and cost of use allocated in accordance with applicable OMB Cost Principles.

F. Provide assurances that the facility:

1) complies (or will comply after completion of renovations) with local licensing and code requirements;

2) will meet the access requirements of the Americans Disabilities Act, and Section 504 of the Rehabilitation Act of 1973;

3) has met the requirements of the Flood Disaster Protection Act of 1973, if applicable.

G. If claiming that the lack of alternative facilities will prevent operation of the program, include a statement of how it was determined that there is a lack of alternative facilities. The statement must be supported by a written statement from a licensed real estate professional in the grantee's service area.

H. Documentation showing the terms (i.e., interest rate, # years, monthly rate, etc.) of any proposed loans related to the purchase, and the repayment plans (detailing balloon payments or other unconventional terms, if any). Include information on all other sources of funding of the purchase, including any restrictions or conditions imposed by other funding sources.

I. Statement of any effects the purchase of the facility will have on the grantee's ability to meet non-federal share requirements. State any intentions to apply for a non-federal share waiver and/or justification if applying for a waiver.

J. Certification by a licensed engineer that the building is structurally sound and safe for use as a Head Start facility (not applicable to modular /portable facilities).

K. Statement of any effects the purchase would have on grantee's ability to stay within the 15% administrative cost limitation. (Note that one-time fees and expenses necessary to the purchase, such as the down payment, the cost of necessary renovation, and loan fees and related expenses, and fees paid to attorneys, engineers, and appraisers, are not considered to be administrative costs.)

L. The proposed schedule for actual acquisition, renovation, and occupancy of the facility.

M. Grantee must provide reasonable assurances that it will obtain a fee simple or such other estate or interest in the site sufficient to assure undisturbed use and possession for the purpose of operating a Head Start program for the useful life of the facility. If the land is not being purchased, grantee must also describe easement, right of way or land rental it will obtain to allow sufficient access to the facility, and to assure continued use of the land.

N. An assessment is needed of the impact of the proposed acquisition on the human environment if it involves significant renovations or significant change in land use, including substantial increases in traffic in the surrounding area due to the provision of Head Start transportation services, pursuant to section 102(2)(C) of the National Environment Policy Act of 1969 (42 U.S.C. 4332(2)(C) and its implementing regulations (40 CFR Part 1500-1508). Also needed is a report showing the results of testing for environmental hazards present in the facility and site (or justification why such testing is not necessary). In addition, such information as may be necessary to comply with the National Historic Preservation Act of 1966 (16 U.S.C. 470f).

O. Assurance that the grantee will comply with the requirements of the Uniform Relocation Assistance and Real Property Acquisition Policies Act of 1970 as amended (42 U.S.C. 4601 et seq. and 49 CFR Part 24) and any costs incurred due to compliance to this Act.

P. A statement of the share (i.e., percentage) of the cost of purchase that will be paid with federal Head Start grant funds.

Q. An independent appraisal of the current value of the facility proposed to be purchased must be included. (Note that the purchase price should be at or lower than the appraised value.)

R. If shared ownership of the facility is proposed, grantee must demonstrate that the prospective co-owner is financially capable of meeting any debt obligations it assumes in connection with the purchase.

S. IN ADDITION TO THE REQUIREMENTS ABOVE, THE FOLLOWING IS REQUIRED FOR PROPOSED PURCHASES OF MODULAR /PORTABLE FACILITIES ONLY:

1) where the unit will be installed (address),

2) if the land where the unit is placed will be purchased by the grantee,

3) If the grantee does not own the land or is not proposing to purchase the land, the application must state who owns the land, and describe the easement, right-of-way or land rental it will obtain to provide allow sufficient access to the modular unit,

4) a statement describing the procurement procedures which will be used to purchase the modular unit, including a copy of the specifications,

5) assurance that grantee will comply with 45 CFR Parts 74 and/or 92, including assurance that all transactions will be conducted in a manner to provide, to the maximum extent practical, open and free competition.

6) Inspection by a licensed engineer or architect within 15 calendar days of installation/completion and submittal of inspection report to the Regional Office within 30 calendar days of the inspection.

T. **The above application requirements are in addition to customary application requirements (i.e., Application for Federal Assistance SF424, policy council approval and application narrative /justification).**

1) NARRATIVE EXPLANATION OF COSTS: To assist the reviewer to determine the allowability of costs, include an explanation of costs included in the analysis. Identify other sources of funds and services donated to acquire or maintain the facility (one-time and on-going), if applicable. Indicate any additional funds, other than one-time funds that will be needed to maintain the facility on an on-going basis.

2) NARRATIVE STATEMENT OF THE NECESSITY FOR THE PURCHASE: Include information that supports the merits of the selected purchase. Address the need for the facility, e.g., expansion, administrative office space, parent training, etc.

3) NON-FEDERAL SHARE INFORMATION: Include proposed non-federal share budget information for any funds being requested to acquire the facility.

4) GRANTEE AGENCY APPROVALS: Include letters of approval signed by Chairpersons from the Policy Council and Board.

12.03 <u>NPRM FOR CONSTRUCTION AND MAJOR RENOVATION</u>

The proposed new regulations for construction and major renovation of Head Start facilities [Exhibit 12.1] include some new definitions:

"Construction" means new building and excludes renovation, alteration, addition, or work of any kind on an already existing building.

"Incidental alteration and renovation" means improvements to a facility which can be readily made, and the total costs do not exceed the lesser of $150,000 or 25% of total direct costs approved for the budget period.

"Major renovation" means structural changes to the foundation, roof, floor, or exterior or load-bearing walls of a facility; or the extension of an existing facility to increase its floor area; or the extensive alteration of an existing facility to significantly change its function and purpose (even if such change does not include any structural changes).

Application requirements are essentially the same as for purchase of a facility, plus a description of the renovations or construction, and a detailed estimate of the costs of the proposed activity. The plans and specifications submitted must also describe the facility as it will be after renovations are complete, and a certification by a licensed engineer or architect as to the <u>cost and technical appropriateness</u> of the proposed renovation or construction must be included. Also, the grantee must certify that upon the completion of major renovation to a facility, or construction of a facility, that inspection by a licensed engineer or architect will be conducted to determine that the facility is <u>structurally sound and safe</u> for use as a Head Start facility.

In order to receive funding for major renovations of a leased facility, the grantee must have a lease that provides for a term of occupancy or at least 5 years or longer from the time the renovation will be complete.

Grantees may not advertise for bids or award a contract for any part of a construction or major renovation funded by grant funds until final working drawings and specifications have been approved by ACF.

All facility construction and major renovation transactions must comply with the procurement procedures in 45 CFR Part 74 and 92, and must be conducted in a manner to provide to the maximum extent practical open and free competition.

All construction and major renovation contracts for facilities acquired with grant funds require the prior written approval of ACF, and shall be on a lump-sum fixed-price basis.

All construction and major renovation contracts for facilities acquired with grant funds shall contain a clause stating that ACF shall have access at all reasonable times to the work being performed pursuant to the contract, at any stage of preparation or progress, and requiring that the contractor shall facilitate such access and inspection.

The grantee must provide and maintain competent and adequate architectural or engineering inspection at the work site to insure that the completed work conforms to the approved plans and specifications. The grantee must submit a final architectural or engineering inspection report of the facility to ACF within 30 days of substantial completion of the construction or renovation.

12.04 DAVIS-BACON ACT

Construction and renovation projects and sub-contracts financed with funds awarded under the Head Start program are subject to the Davis-Bacon Act and the regulations of the federal Department of Labor (DOL).

The Davis-Bacon Act requires that any contractor hired to construct, renovate, or repair a Head Start facility (if the contract exceeds $2,000) must pay the laborers and mechanics engaged in the construction, renovation, or repair "prevailing rate wages."

Therefore, the grantee must provide an assurance that all laborers and mechanics employed by contractors or sub-contractors in the construction or renovation of affected Head Start facilities shall be paid wages at not less than those prevailing on similar construction in the locality, as determined by the Secretary of Labor.

These prevailing rate wages are determined by DOL for each county in the country and are updated, as necessary.

The Davis-Bacon Act also includes provisions about fringe benefits to be paid to laborers and mechanics, limitations on wage withholding, and payroll and record keeping requirements.

ACF issued a memorandum, ACYF-IM-HS-04, titled "The Davis-Bacon Act and Head Start Programs" [Exhibit 12.3], which provides guidance on the Davis-Bacon Act, including the general features and definitions of the Act, and our roles in monitoring compliance with it. The memo also answers questions regarding Davis-Bacon implementation by grantees, and includes the DOL Payroll Form and Compliance Certification.

12.05 FACILITY REFERRAL AND INFORMATION SERVICE (FRIS)

The Facility Referral and Information Service (FRIS) has been established by the ACF Head Start Bureau to provide referrals to a wide-range of resources related to Head Start facilities. Included in these services is information on prevailing wage rates as mandated by the Davis-Bacon Act.

The FRIS can be contacted at (800) 303-0705, or fax at (301) 309-2084, or via e-mail: kcostigan@acf.HHS.gov.

CHAPTER 13

FINANCIAL REPORTS

13.01 <u>REPORTING - GENERAL</u>

The financial and business management aspects of ACF grants are continuously monitored and reviewed through the collection and assessment of information about the grantee gathered from audits, financial status reports, site visits, and continuation grant applications; as well as through correspondence, grantee Board and committee meeting minutes, newspaper articles, and other sources.

In exercising its stewardship responsibilities, ACF requires that all grantees employ sound financial and business management practices to ensure that grant program objectives are met. ACF also recognizes that grantee organizations vary widely in their demonstrated business management capability, and in their ability to exercise prudent stewardship of federal funds.

In accordance with federal regulations, 45 CFR 74.52 "Financial Reporting," grantees are required to submit financial information to ACF for each budget period on "Financial Status Report" form SF-269.

13.02 <u>FINANCIAL STATUS REPORTS (SF-269)</u>

All ACF grantees must use the SF-269, "Financial Status Report" to report the status of grant funds.

Each grantee must report program outlays/expenditures and program income on the same accounting basis (i.e., cash or accrual) which it uses in its own accounting system.

Information reported <u>must</u> be reconcilable to the grantee organization's accounting records.

Exhibit 13.1 is a copy of the SF-269 document and the line-by-line instructions for completion of the form.

Additional information is requested on the final Head Start SF-269's, which must be placed in the "Remarks" section of the form. The additional information is related to reimbursement by USDA of food costs, total training and technical assistance costs, total disabilities services costs, and total administrative costs. ACF issued two memorandums regarding this additional information requirement, Region VI-OFO-90-1 and ACYF-PI-90-06, which are included as Exhibits 13.2 and 13.3.

The SF-269's must be signed by an appropriately authorized grantee official. In general, this will be the Board Chairperson (or President or Superintendent) unless the Executive Director has been formally authorized to sign legal documents for the agency. The forms should <u>not</u> be signed by the fiscal officer or auditor, even if that individual is the one providing the figures for the form.

The final SF-269 must be reconciled by the auditor to the final audit report for the year. If the audit period is different from the budget period covered by the SF-269, a footnote or additional page should be added to the audit to show the reconciliation of the audit figures with the final SF-269. If the SF-269 needs to be amended, based on the audit, then an amended SF-269 should be sent to ACF as soon as possible.

The final SF-269 should also be reconciled by the grantee to the figures on the PMS-272 "Cash Transactions Report" for the final quarter of the budget period.

13.03 <u>DUE DATES FOR REPORTS</u>

ACF grantees must submit 2 semi-annual SF-269's, due no more than 30 days after the end of the first and last 6-months of each annual budget period.

Grantees must also submit a final SF-269, due no more than 90 days after the end of each project period. For grantees with indefinite project periods, like Head Start, the final SF-269 is due no more than 90 days after the end of each annual budget period.

13.04 ACTION ON OVERDUE REPORTS

If neither the report nor an acceptable explanation is received, ACF may issue a letter to the grantee stating that the report must be received within 30 days, and that failure to do so could result in:

- Suspension or termination of the grant;
- Withholding of any additional grant funds; or
- Additional and more severe enforcement actions.

The Regional Grants Officer, in consultation with the Program Office, may take any of the following additional actions when a grantee is delinquent in submitting a report:

- Withhold further grant funds;
- Convert the grantee to the reimbursement method of payment (instead of the usual advance payment method);
- Withhold any additional awards otherwise approved and pending for the grant project;
- Request a special audit by the HHS/Office of Inspector General;
- Notify other federal granting agencies of the delinquency so that precautionary measures may be taken;
- While the report is overdue, award no discretionary grant funds under any other ACF projects conducted by the grantee organization;
- Consider legal action with the HHS/Office of General Counsel; or
- Designate the grantee as "High Risk."

CHAPTER 14

RECORDS RETENTION

14.01 RETENTION REQUIREMENTS

Grantee financial records, supporting documents, statistical records, and all other records pertaining to the grant award, must be retained for a period of at least 3 years from the date of submission of the annual financial report.

The only exceptions are the following:

- If any litigation, claim, financial management review, or audit is started before the expiration of the 3-year period, the records must be retained until all litigation, claims, or audit findings involving the records have been resolved and final action taken.
- Records for real property and equipment acquired with federal grant funds must be retained for 3 years beyond the date of final disposition (i.e., the date the equipment or property was sold or otherwise disposed).
- Indirect cost rate proposals and computations, cost allocation plans, and any similar accounting computations of the rate at which a group of costs is chargeable (such as computer usage charges, or composite fringe benefit rates):

  1) If the proposal, plan, or computation was submitted by the grantee to the federal government, then the 3-year retention period for the grantee's supporting records (for the proposal, plan, or computation) starts on the date of such submission.

  2) If the grantee was not required to submit the plan, proposal, or computation to the federal government, then the 3-year retention period starts at the end of the fiscal year covered by the proposal, plan or computation.

Copies of original records may be substituted for the originals only if approved and authorized by ACF.

14.02 ACCESS REQUIREMENTS

ACF, as the HHS awarding agency (and the HHS/Office of Inspector General (OIG), the U.S. Comptroller General (GAO), or any of their duly authorized representatives) has the right of timely and unrestricted access to any of the grantee's books, documents, papers, or other records of the grantee's that are pertinent to the grant award, in order to make audits, reviews, examinations, excerpts, transcripts, and/or copies of such documents.

This right also includes timely and reasonable access to all of a grantee's personnel for the purpose of interview and discussion related to such documents.

The rights of access to records and to personnel are for as long as the records are retained, and are not limited to the required retention period.

14.03 COMPUTERIZED RECORDS

If grantees choose to maintain computerized records, the same requirements still apply. The "computer age" does not change the fact that grantee financial report information and business management practices must be based on verifiable supporting documents and records.

Grantees must have supporting records for accounting, auditing, and financial status reports. Some of our ACF grantees have indicated that they are not printing out monthly (or even annual in some cases) general ledgers or other accounting records, but are instead maintaining all of their information in the computer systems. Therefore, for these grantees, the computerized records must be transferred or copied to diskettes at the applicable "points in time" which reflect the figures for those reports.

In addition, the diskettes must then be carefully maintained and the data periodically re-saved or whatever is necessary for the records to remain verifiable and accessible to ACF throughout the required retention period.

Also, if computer systems are upgraded and/or changed and the old records can only be accessed using the old system, then a copy must be maintained somewhere of the old system, or some other mechanism must be devised in order for the records to remain accessible for the required retention period.

CHAPTER 15

AUDIT REQUIREMENTS

15.01 GENERAL

All ACF grantees, whether non-profit organizations, local or tribal governments, or universities, are subject to the Single Audit Act Amendments of 1996. This means that all of our grantees are required to have an annual audit performed, and the audit must be performed in accordance with the requirements of OMB Circular A-133 "Audits of States, Local Governments, and Non-Profit Organizations," dated June 24, 1997 [Exhibit 15.1].

The only exception is that organizations that expend a total of less than $300,000 per year in federal funds from all sources are exempt from the federal audit requirements for that year, but grantee records must still be made available for review or audit by ACF, or other federal representatives.

15.02 OMB CIRCULAR A-133 REQUIREMENTS

The revised version of OMB Circular A-133, published June 24, 1997, provides uniform single audit requirements for all non-federal grantees - state and local governments (including tribal governments), colleges and universities, hospitals, and non-profit organizations. It supersedes past versions of Circular A-133, and replaces Circular A-128, "Audits of State and Local Governments."

Grantees should be aware of some of the revisions to the audit process under Circular A-133 which affect:

- Compliance and reporting responsibilities;
- Audit threshold and approach;
- Audit reporting package;
- Data collection form (SF-SAC).

15.03 COMPLIANCE AND REPORTING RESPONSIBILITIES

Under the new audit requirements, all grantees are responsible for:

- Identifying all federal awards received and the amounts expended for each program;
- Maintaining internal controls to assure compliance with regulations, laws, and grant requirements and provisions;
- Complying with relevant laws, regulations, and grant provisions;
- Preparing financial statements, including the schedule of expenditures of federal awards;
- Ensuring that the audits are properly conducted and reports submitted on time; and
- Following up on audit findings, and taking necessary corrective actions.

Grantees are now responsible for the follow-up on audit findings, which includes preparing a summary schedule of any prior audit findings, and taking the necessary steps to resolve current year findings based on a corrective action plan. In the "Summary Schedule of Prior Audit Findings," grantees must indicate, for each one of the prior-year findings, whether it has been corrected, not corrected, or is no longer valid. (A finding is "invalid" only if, after two years, no federal agency or pass-through entity has followed up or issued a management decision regarding the finding.) If a valid finding has not been corrected, the grantee must indicate its planned corrective actions.

A corrective action plan, prepared by the grantee at the end of the audit, should address each current-year finding in the auditor's report, and include (for each finding): the name of the contact person responsible for taking corrective action, the specific actions planned to correct each finding, and the anticipated completion date each finding will be corrected. If the grantee does not agree with one of the audit findings or believes no corrective action needs to be taken for that finding, the grantee should include an explanation in the corrective action plan.

15.04 AUDIT THRESHOLD AND APPROACH

Two of the most significant changes involve the raised audit threshold and the risk-based approach to audits. Under the revised threshold provisions, only a grantee that expends $300,000 or more in federal funds for the year must have a single audit performed. Grantees that expend less than $300,000 in federal awards for a particular year, are exempt from federal audit requirements, although their records must still be available for federal review. Grantees are still responsible for monitoring their sub-recipients/delegates, regardless of the amount expended.

Under the risk-based approach, auditors make an overall assessment of the risk of a serious non-compliance occurring, which could then have a material effect on one of the grantee's federal programs. The risk-based approach to audit shifts the focus of the audit to the major programs, in order to test grantee compliance and internal controls over primarily the largest of their federal awards. Auditors will use the new approach (described thoroughly in Circular A-133) to determine which programs are "major," which will then determine which programs get audited. If the auditor determines that the grantee has no "major" programs, then those federal programs with awards that make up at least 50% of the grantee's total would be the programs audited (called "percentage of coverage rule").

Using the risk-based approach, auditors will also consider current and prior audit experiences, the level of oversight by the federal awarding agencies, and the inherent risk of particular types of programs.

15.05 AUDIT REPORTING PACKAGE

Grantees (not their auditors) are responsible for, and required to submit, a reporting package that contains information about their organization, all the federal awards they administer, and the audit results (based on auditor's report) regarding audit findings and questioned costs.

The annual reporting package must now include:

- An audit certificate with concise, general statements about the audit results, signed by the grantee's Board Chairperson;
- The financial statements and schedule of expenditures of all federal awards (prepared by the grantee);
- The audit reports and schedule of findings and questioned costs (prepared by the auditor);
- The summary schedule of prior audit findings (prepared by the grantee); and
- A corrective action plan, addressing current and prior findings (prepared by the grantee).

The deadline for submitting the audit reporting package is now 9 months (instead of 13 months) from the end of the period audited, or 30 days after the grantee receives the auditor's report, whichever is earlier.

15.06 DATA COLLECTION FORM (SF-SAC)

Grantees are also now required to complete a data collection form (SF-SAC), to be sent along with the audit reporting package, to the Federal Audit Clearinghouse. Information on the data collection form will be used to establish a government-wide audit database. The database will contain information on federal grantees, federal awards, and audit results. The auditor will prepare and sign certain sections of the SAC form that deal with audit results and federal awards. However, grantees must sign the form as well, certifying to the audit's completeness and accuracy. A copy of the form is provided as Exhibit 15.1.

Grantees will indicate on the SF-SAC form which federal agencies should receive copies of the audit report (i.e., only the agencies affected by the audit findings), and provide the required number of report copies to the Clearinghouse for them to distribute.

15.07 FEDERAL AUDIT CLEARINGHOUSE

The entire audit reporting package should now be mailed to the federal Audit Clearinghouse (not to the OIG in Kansas City), and one courtesy copy should be sent to the ACF Regional Office.

The address for the federal Audit Clearinghouse is:

Single Audit Clearinghouse
1201 E. 10th Street
Jeffersonville, IN 47132

The address to send the courtesy copy to is:

Janice Pruitt, Regional Grants Officer
Administration for Children & Families
1301 Young Street, Room 937
Dallas, TX 75202

For questions concerning the submission process, the audit reporting package, or the SF-SAC form, grantees and auditors should contact the federal Audit Clearinghouse at 1-888-222-9907. Information can also be found on the internet at: http://harvester.census.gov/sac.

CHAPTER 16

INTERNAL CONTROLS

16.01 GENERAL

Plans and procedures designed to meet the need for controlling financial operations are called "internal control." A grantee's internal control system is made up of the plan of the organization, and whatever methods and procedures are used by the organization to:

- Safeguard its assets;
- Produce accurate accounting data and reports;
- Contribute to efficient operation of the agency; and
- Encourage staff to adhere to management policies and grant requirements.

Internal control, in principle, is a plan of organization under which employees' duties are so arranged, and records and procedures are so designed, as to make it possible to exercise effective control over assets, liabilities, resources, and expenditures.

An internal control system basically involves:

1. Division of responsibility among different employees for a sequence of related functions, so that no one person has control from beginning to end of a process;
2. Clear establishment of each employee's responsibilities and duties;
3. Separation of the responsibility for maintaining records, from the responsibility for operations, acquisitions, and custody of assets; and
4. Use of proofs, checks, sign-offs, and other security measures.

16.02 PURPOSE AND IMPORTANCE

The purpose of internal control is to protect the money and other assets of the grantee organization against employee error or dishonesty. Although it may be proper to assume that all of the employees are honest, it is still unfair for grantees to permit weaknesses in their accounting controls to tempt employees toward dishonesty. An adequate system of internal control promotes compliance with grant conditions, regulations, and grantee internal policies; prevents illegal or unauthorized transactions or acts; and provides proper accounting data and information with a minimum of human error.

A sound internal control system also protects the grantee organization's employees against unwarranted allegations of dishonesty, by fixing responsibility and by removing causes of employee temptation. Sound internal controls benefit the grantee, its employees, the funding sources, and the auditors, by the proper control of financial transactions.

16.03 SEGREGATION OF DUTIES AND RESPONSIBILITIES

An adequate system of internal control will provide for the separation of employees' work so that no one employee performs a complete cycle of operations. For example, if employees who initiate transactions also record the transactions, the control function of general ledger accounting would be lost.

The segregation of the operating employee's duties (including responsibility for acquisition, custody, and disposition of assets) from the accounting employee's duties (of recording and posting transactions) is another basis of strong internal control.

The clear definition of each employee's responsibilities and duties in the sequence of operations and record keeping is another essential. The duties and responsibilities of each position in the organizational structure should be clearly defined in writing. There must be no doubt, for example, as to which employee is responsible for coding transactions to the proper account, which one is responsible for verifying invoice prices and computations, and which one is responsible for approving invoices for payment.

Proper separation of duties and responsibilities should result in the creation of a chain of documentary evidence for each transaction, consisting of written approvals by key employees.

A short list of examples of appropriate separation of duties and responsibilities is provided at the end of this chapter, as Exhibit 16.1 "Sample Segregation of Duties."

A copy of the "Checklists for Internal Control" from the old HDS Grants Manual has also been provided as Exhibit 16.2.

16.04 INTERNAL CONTROL IN SMALLER ORGANIZATIONS

Small organizations (those with one bookkeeper or accountant and few other employees) will find it difficult to establish a division of employee duties and responsibilities that result in strong internal control.

In order to establish the soundest possible system of internal control, it will be necessary for others in the organization to perform some functions. For example, the Executive Director could perform some functions, the bookkeeper could perform some, and other persons (such as the office secretary or the program director) could perform others.

Small organizations should carefully develop all possible internal control techniques and procedures utilizing the advice of their financial counsel and/or auditor.