

CONTRACT AUDIT CIRCULAR No. MPO - 2



OHIO DEPARTMENT OF TRANSPORTATION

CENTRAL OFFICE, 1980 W. Broad St., 4th Floor, COLUMBUS, OHIO 43223

SUBJECT: Submittal of Cost Allocation Plans; Required Documentation;
Treatment of Unallowable Costs and Erroneous Payments

Effective Date: July 1, 2010

Last Updated: April 1, 2010

I. DEFINITIONS

As used in these Ohio Department of Transportation (ODOT) MPO Contract Audit Circulars—

1. The "*Code of Federal Regulations*" (CFR) is the codification of the general and permanent rules published in the *Federal Register* by the executive departments and agencies of the Federal Government. The CFR is divided into 50 titles that represent broad areas subject to Federal regulation. 49 CFR Chapter 18 (Common Rule) sets forth the uniform administrative rules for Federal grants and cooperative agreements and subawards to State and Local governments.
2. "OMB Circular A-87, *Cost Principles for State, Local, and Indian Tribal Governments*," establishes the principles and standards for determining costs for Federal awards carried out through grants, cost reimbursement contracts, and other agreements with State and Local governments. The Circular is issued by the Office of Management and Budget, an Executive Office of the President of the United States.
3. "Cognizant agency" refers to the Federal agency responsible for negotiating and approving indirect cost rates for a non-profit organization on behalf of all Federal agencies that provide funds to that organization. The cognizant agency for non-profit organizations is determined by calculating which Federal agency provides the most grant funding.
4. "Incurred Cost" refers to the various elements of total cost submitted on the MPO agency's overhead schedule or invoices. Costs may be categorized as either: (a) Direct labor, (b) Fringe benefits, (c) Indirect, or (d) Other direct.
5. An "incurred cost audit" involves an examination of the accounting records and source documents that support submitted costs billed against Federal-aid contracts. The examination also includes an assessment of the auditee's internal controls, timekeeping practices, and general operating policies.
6. "Internal Controls" are policies, procedures, and activities designed to help an organization achieve its management objectives, safeguard resources, report reliable information, and comply with applicable laws. While internal controls cannot completely eliminate the risk of error, fraud, or mismanagement, well-conceived procedures and a good control environment can minimize the potential for abuse.
7. "Professional and consultant service fees" represent costs of services rendered by persons who are members of a particular profession or who possess special skills and who are not officers or employees of the MPO agency. Such costs include those of outside accountants, lawyers, actuaries, and consultants.

8. A "Cost Allocation Plan" (CAP) is a series of documents that summarizes, in writing, the methods and procedures that an organization will use to allocate costs to various programs, grants, contracts and agreements. It includes, but is not limited to, a "Statement of Direct Labor, Fringe Benefits, and General Overhead". In this circular, the term "Indirect Cost Rate Proposal" is used synonymously with "Cost Allocation Plan."
9. A "Statement of Direct Labor, Fringe Benefits, and General Overhead" is a schedule that shows details regarding an MPO agency's estimated-to-actual total incurred costs for an accounting period. For enhanced readability, in these Contract Audit Circulars the term "overhead schedule" is used synonymously with "Statement of Direct Labor, Fringe Benefits, and General Overhead."
10. An "Overhead rate" is comprised of two components: a) the Fringe Benefits cost rate and b) the Indirect Cost rate.
11. The "Fringe Benefits cost rate" is the total of all fringe benefits costs (e.g., all leave types, employer retirement contributions, employer payroll taxes, health-related insurance costs, etc.) divided by the total labor (direct and indirect) costs.
12. The "Indirect Cost rate" is the total of all indirect costs (e.g., indirect labor, indirect labor fringe benefits, building occupancy costs, miscellaneous materials and supplies, equipment, etc.) divided by either: a) direct labor costs or b) direct labor costs plus direct labor fringe benefits costs.

II. AUTHORITY

ODOT's authority to conduct incurred-cost audits is granted by 49 CFR 18.42, which provides that the awarding agency or its designee, shall have the right of access to any pertinent books, documents, papers, or other records of grantees and subgrantees which are pertinent to a grant funded in whole or in part with Federal funds.

III. COGNIZANCY

The Federal Highway Administration (US DOT) is the cognizant agency for most Ohio MPO agencies. Acting as the Oversight Agency, the Ohio Department of Transportation performs cognizant agency responsibilities for MPO agencies located fully within Ohio's boundaries and for bi-state MPO agencies where Ohio is the lead state. The Ohio Department of Transportation reviews, negotiates, and approves cost allocation plans for these MPO agencies.

For MPO agencies where FHWA is not the cognizant agency or for bi-state MPO agencies where Ohio is not the lead state, the MPO agency must comply with Section VI.- *Application* of this audit circular.

IV. ISSUE

During the review and approval of an MPO agency's overhead rate, the auditor must determine whether the indirect costs proposed by an MPO agency are allowable, allocable, and reasonable. To facilitate the review and approval process, key documentation is required to ensure that costs comply with applicable federal and state guidelines.

V. ALLOWABILITY

To claim indirect costs under Federal awards, an MPO agency must prepare an annual Cost Allocation Plan to support its indirect costs. The proposal and related documents must be retained for audit in accordance with the records retention requirement contained in 48 CFR 18.

Attachment E, Section D, of OMB Circular A-87, *Cost Principles for State, Local and Indian Tribal Governments*, provides the conceptual framework regarding the –

- (1) preparation of a Cost Allocation Plan;
- (2) timeline for submittal;
- (3) documentation;
- (4) certifications;
- (5) submittal; and
- (6) negotiation and approval process.

VI. APPLICATION

A. Generally

The MPO agency must prepare and submit an annual Cost Allocation Plan proposal to ODOT for review, negotiation and approval. The CAP is a series of documents that summarizes, in writing, the methods and procedures that an organization will use to allocate costs to various programs, grants, contracts and agreements.

The CAP must be developed and submitted to the Office of Audits no less than four (4) months prior to the start of the MPO agency's fiscal year, unless an exception is requested in writing and approved by ODOT. (See Attachment 2.2).

B. Annual CAP Documentation

The MPO agency must submit the following documents to support its claim for indirect costs. ODOT prefers the electronic submission of all documentation –

- (1) An overhead schedule, including subsidiary worksheets and other relevant data, cross-referenced and reconciled to the financial records of the MPO agency.
- (2) Allocated central services costs must be supported by a summary table.
- (3) A copy of the financial statements (preferably audited) upon which the rate is based. Adjustments resulting from the use of unaudited data will be recognized, where appropriate, by ODOT in a subsequent proposal.
- (4) A schedule that discloses the direct labor base for all government awards. The costs should be detailed between salaries and wages and other direct costs. (See Attachment 2.3).
- (5) Documentation that details the standardized treatment of costs as either a direct or indirect expense.
- (6) An organization chart that correctly details the structure of the agency during the period for which the proposal applies, along with a functional statement noting the duties and responsibilities of all units that comprise the agency.
- (7) A completed and signed original Certification of Indirect Costs statement. (See Attachment 2.1). While this document may be submitted electronically, an original must also be sent to ODOT for inclusion in the MPO agency's permanent audit file.
- (8) For the MPO agencies where ODOT does not act as cognizant agency, a copy of the approved written agreement establishing the fringe and indirect cost rates to be used for the period.

C. Negotiation and Approval of Rates

For MPO agencies where ODOT acts as cognizant agency, ODOT will review and approve estimated fringe and indirect cost rates for use by the MPO agency for the fiscal year. Once approved, the MPO agency must use the same rates for all grants during the period.

- (1) For MPO agencies where ODOT acts as cognizant agency, ODOT will formalize in a written agreement the fringe and indirect cost rates to be used for the period. The agreement will be subject to re-opening if it is subsequently found to violate a statute, or the information upon which the plan was negotiated is later found to be materially incomplete or inaccurate.
- (2) The MPO agency may not unilaterally increase or decrease the estimated fringe and indirect cost rates once approved by ODOT. The MPO agency should contact the ODOT Office of Audits for guidance if subsequent events create the potential for a material over or under recovery for the period.
- (3) The MPO agency must use the approved fringe and indirect cost rates to allocate costs to all programs. This will ensure that each program is allocated its proportionate share of the overhead costs, regardless if eligible for reimbursement.

D. Application of Overhead Rates

During the course of an audit, an erroneous payment or unallowable cost may be determined. The treatment of each is discussed below:

- (1) Erroneous payment of a direct cost by an ODOT/FHWA program – The entity will be required to reimburse ODOT for the federal and state share of the erroneous payment. In accordance with 49 CFR 18, interest may be charged in compliance with the Federal Claims Collection Standards.¹
- (2) Inclusion of an unallowable cost as a component of the indirect cost rate – The entity will be required to record a credit to the financial system for the total unallowable costs identified during the audit. If the financial system is still open for the year under audit, the credit will be charged to that year. However, in most likelihood, the year under audit will have been closed. In this event, the credit will be charged to the open, active fiscal year. The fringe cost pool or the indirect cost pool will be credited for the unallowable cost, as appropriate. The entity must document the credit to demonstrate recognition of the unallowable cost.

E. Monthly Reimbursement Billing Process

In accordance with ODOT Standard Procedure 322-003 (SP), the MPO agency submits monthly invoices to the ODOT District office for reimbursement of costs incurred to conduct the various FHWA and ODOT funded work program activities. In compliance with this procedure, the MPO agency prepares a monthly summary invoice for each ODOT PID using a standard Excel template approved by ODOT. Supporting reports attached by the MPO agency to each invoice provide details of costs incurred during the period. The supporting reports include the Current Period and Cumulative Cost Reports. These reports are also known as the "Distribution of Costs Claimed Report" and the "Program Financial Status Report".

¹ The Federal Claims Collection Standards are available at 4 CFR Ch. II.

F. Electronic Submission of Annual Reports

The MPO agency must prepare the monthly Current Period and the Cumulative Cost Reports, referred to in section E above, using Excel spreadsheets and annually submit the Excel workbook to the ODOT Office of Audits within 90 days after the end of the MPO agency's fiscal year. The reports are to be prepared by the MPO agency consistent with the following parameters:

- (1) One Excel workbook file will be prepared per fiscal year.
- (2) Within the Excel workbook one worksheet will be prepared per PID.
- (3) Each Excel worksheet will contain all twelve of the monthly cost reports for the PID, for the fiscal year. In addition, for MPO agencies using the Provisional Rate Method, the year-end adjusting cost report must also be included in the worksheet as cost report number 13.
- (4) The monthly cost reports must be sequentially aligned from left to right within the worksheet. For MPO agencies using the Provisional Rate Method, the year-end adjusting cost report must be placed at the end of the monthly sequence, as cost report number 13, prior to the annual total cost report.
- (5) The annual total cost report must accumulate the costs for the entire fiscal year from all the monthly reports, including the cost report number 13.
- (6) Excel formulas must be used at appropriate locations to calculate row and column totals.
- (7) The fiscal year period must match the MPO agency's fiscal year. For agencies with a December 31 fiscal year end, the reports will cover the January through December period, and for agencies with a June 30 fiscal year end, the reports will cover the July through June period.

A sample of the required format for the monthly reports is provided as Attachment 2.4 for entities that are not familiar with this reporting format.

VI. REFERENCES

- OMB Circular A-87, Attachment E, Section D, of OMB Circular A-87, *Cost Principles for State, Local and Indian Tribal Governments*
- OMB Circular A-87, Attachment A, Section C (3) (Determining Allocability)
- ODOT Contract Audit Circular No. MPO – 1, *Definitions, Audit Authority, and Guidance for Computing Overhead Rates*
- ODOT Standard Procedure 322-003 (SP), *Financial Reimbursement for Local Public Agencies (LPA) Managing the Metropolitan Transportation Planning Process and Other Work Program Activities*