Management Matters
A PMFO Series

Cost Allocation

National Center on Program Management and Fiscal Operations (PMFO)
Objectives

• Discuss reasons
• Deepen your knowledge of cost allocation
• Define key cost terms
• Describe a step-by-step process for developing a cost allocation plan

What is Cost Allocation?

The *process* of assigning to two or more programs the shared cost of an item or service.
Why is it Necessary?

The federal government should only bear its fair share of costs.
- Federal Cost Principles

Cost Principles

To be allowable, costs must be:

- Reasonable
- Allocable
- Receive consistent treatment
- Conform to award limitations or exclusions
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Key Cost Allocation Terms

Reasonable

• The cost is necessary for performance of award and a prudent person would pay the same amount for an item under similar circumstances

Allocable

• The cost can be assigned to the award because it benefits the program
Which of the Cost Principles Apply to my Program?

• 2 CFR Parts 215 & 220: Educational Institutions

• 2 CFR Part 225: State & Local Governments

• 2 CFR Part 230: Non-Profit Organizations
Which of the Cost Principles Apply to my Program?

• 2 CFR Parts 215 & 220: Educational Institutions

• 2 CFR Part 225: State & Local Governments

• 2 CFR Part 230: Non-Profit Organizations
Direct Costs

Costs which clearly and directly benefit the implementation of a program or service. Direct costs may pertain to one program, or be shared across multiple programs.

Examples of Direct Costs
Head Start classroom furnishings and supplies

Bus to transport Head Start children
Teacher salaries

Teacher Salaries Examples
Indirect Costs

Indirect Costs are incurred for common or joint objectives, and cannot be readily identified with one program.

Examples of Indirect Costs

- Executive Director Salary
- Auditing services
- Administrative supplies
Examples of Indirect Costs

• Executive Director Salary
• Auditing services
• Administrative supplies
Programs with Multiple Funding Sources Need a Cost Allocation Plan

What is a Cost Allocation Plan?

The *method* to fairly and equitably allocate shared costs
Step 1: Direct and Shared Expenses

★ Identify all costs and services which benefit only one program. These do not have to be allocated.

★ Identify all costs and services shared between Head Start and Early Head Start or between either program and another type of program.

Step 2: Classify Shared Expenses

★ For each shared expense, determine if it is:
  – Shared, but can be distributed by benefit to each program
  – Shared, but difficult to assign benefit to a particular program
Step 3: Categorize

- Initially, combine shared expenses into broad categories, such as:
  - Personnel (salaries and fringe benefits)
  - Facilities (grantee owned, leased, donated)
  - Equipment (especially buses)
  - Service contracts (janitorial, maintenance)
  - Other shared expenses

Step 4: Basis for Allocation

- Within the broad categories, consider how the grantee operates its programs and how shared expenses vary within categories.

- Identify a reasonable basis for allocating costs within each category and variation, i.e. hours worked, children served, services provided.
Step 5: Create the Plan

★ Once categories, variations and a reasonable basis for allocation are identified, you are ready to create the cost allocation plan.

★ The more thought you put into how the plan will function, the more accurate the plan will be.

Shared Facilities

<table>
<thead>
<tr>
<th></th>
<th>Head Start</th>
<th>Early Head Start</th>
<th>Adult Basic Ed</th>
</tr>
</thead>
<tbody>
<tr>
<td>Classrooms</td>
<td>3,000</td>
<td></td>
<td>2,000</td>
</tr>
<tr>
<td>Offices</td>
<td></td>
<td>2,000</td>
<td></td>
</tr>
<tr>
<td>Meeting Room</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>• 30 hours ABE (75%)</td>
<td>250</td>
<td>750</td>
<td></td>
</tr>
<tr>
<td>• 10 hours EHS (25%)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Subtotals:</td>
<td>3,000</td>
<td>2,250</td>
<td>2,750</td>
</tr>
<tr>
<td>Percentages:</td>
<td>37.5%</td>
<td>28.0%</td>
<td>34.5%</td>
</tr>
<tr>
<td>Common Area-2,000 sq ft</td>
<td>750</td>
<td>560</td>
<td>690</td>
</tr>
<tr>
<td>Entire Center:</td>
<td>3,750</td>
<td>2,810</td>
<td>3,440</td>
</tr>
<tr>
<td>Total:</td>
<td></td>
<td></td>
<td>10,000</td>
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</tbody>
</table>
Bus Cost Allocation Plan

<table>
<thead>
<tr>
<th>Trip No.</th>
<th>Mileage</th>
<th>Head Start</th>
<th>Public School</th>
</tr>
</thead>
<tbody>
<tr>
<td>Morning Route</td>
<td>80</td>
<td>10</td>
<td>20</td>
</tr>
<tr>
<td>2:00 pm Route</td>
<td>80</td>
<td>10</td>
<td>None</td>
</tr>
<tr>
<td>3:30 pm Route</td>
<td>80</td>
<td>None</td>
<td>20</td>
</tr>
<tr>
<td>Totals:</td>
<td>240</td>
<td>20</td>
<td>40</td>
</tr>
<tr>
<td>Percentage used:</td>
<td>n/a</td>
<td>33.3%</td>
<td>66.7%</td>
</tr>
<tr>
<td>Cost per day:</td>
<td>n/a</td>
<td>240 x $1.32=$316.80</td>
<td>240 x $1.32=$316.80</td>
</tr>
<tr>
<td></td>
<td></td>
<td>.333 x $316.80=$105.50</td>
<td>.667 x $316.80=$211.30</td>
</tr>
</tbody>
</table>

Considerations for Allocation of Buses and Vehicles
- Reason for use of vehicle
- Operating cost
- Cost per mile
- Number of passengers
- Make-up of passengers

Cost Allocation Planning Summary

Define who, what, when, where, and how the agency provides services

Identify what costs are direct and what costs need to be allocated

Categorize shared costs
Cost Allocation Planning Summary

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Identify what costs are direct and what costs need to be allocated.

Categorize shared costs.
Cost Allocation Planning Summary (cont.)

- **Develop** allocation methods based on actual agency operations

- Periodically **review** for accuracy and consistency

- **Update** cost allocation plans as plans change
Cost Allocation Planning Summary (cont.)

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- Periodically review for accuracy and consistency
- **Update** cost allocation plans as plans change

Cost Allocation Red Flags

- Different cost categories allocated the same way
- HS/EHS program charged disproportionately or in response to funding losses in other programs
- Allocations of similar expenses vary from year to year
- Double charging both direct and indirect costs
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Cost Allocation Tips

- Staff allocations match time sheets, payroll and personnel activity reports
- Allocations are consistent with job descriptions
- Program changes are reflected in allocation plan.
- Cost allocation plan is documented.
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