



Frequently Asked Questions about Indirect Costs

Responses to frequently asked questions (FAQs) regarding the indirect cost process and indirect cost rates.

In addition to these indirect cost and indirect cost rate FAQs, information on the indirect cost process is also available in Procedure 915 of the [*California School Accounting Manual \(CSAM\)*](#), which may be viewed and printed.

1. What governs indirect cost rates for local educational agencies?

The United States Department of Education (ED) has approved a delegation agreement with the California Department of Education (CDE) that authorizes the CDE to establish indirect cost rates for California's local educational agencies (LEAs). Following is pertinent information concerning the agreement:

- Delegation Agreement Number: 2010-163
- Effective Period: July 1, 2010, to June 30, 2015, for rates approved for use in fiscal years 2011–12 through 2016–17.
- Type of Indirect Cost Rate: Fixed Rate (with a carry-forward provision)
- Indirect Cost Rate Category: Restricted (computed per 34 *Code of Federal Regulations (CFR)* 76.564)
- Term Covered by the Rate: Indirect cost rates cover a one-year period and are calculated and approved annually.
- Use of Rate: Indirect cost rates are for use in the award and management of federal (and state) contracts, grants, and other assistance arrangements governed by Office of Management and Budget (OMB) Circular A-87 (superseded by Uniform Guidance 2 *CFR* part 200 for grants awarded after December 26, 2014) and Education Department General Administrative Regulations (EDGAR) 34 *CFR* parts 75.561 and 76.561(b) and (c).

2. What are indirect costs?

Indirect costs are agency-wide, general management costs (i.e., activities for the direction and control of the agency as a whole). General management costs consist of administrative activities necessary for the general operation of the agency, such as accounting, budgeting, payroll

preparation, personnel services, purchasing, and centralized data processing.

Conversely, direct costs are costs that provide measurable, direct benefits to particular programs. For LEAs, these can include costs that relate directly to instructional programs and also support costs that relate to the peripheral services necessary to maintain the instructional programs. Examples of LEA direct costs include salaries and benefits of teachers and instructional aides, payments for textbooks, instructional supply purchases, and pupil service costs (e.g., counseling, health services, pupil transportation).

3. What is an indirect cost rate?

In general terms, an indirect cost rate is the percentage of an organization's indirect costs to its direct costs and is a standardized method of charging individual programs for their share of indirect costs.

4. Why use an indirect cost rate? How does it benefit an organization?

General management costs are necessary for any program to exist. For instance, all programs will use the business office at one time or another for services such as contracts, purchasing, payroll checks, and personnel management. Without the benefit of an indirect cost rate, there would be no standard way for each program to contribute its share of the general management costs without spending a lot of staff time having to "time account" to each activity. By using an indirect cost rate, LEAs have a standardized, efficient way to recover a share of general management costs from individual programs.

5. I hear that indirect costs cannot be charged on certain types of costs. What are these costs and why can I not charge indirect costs against them?

Certain types of costs (activities) require relatively minimal administrative support compared to the amount of dollars spent. These costs would distort the indirect cost process and are excluded from the calculation of the indirect cost rate. Following are the most common costs excluded from the calculation:

Subagreements for Services (object 5100), which include expenditures for subagreements and subawards pursuant to certain contracts, subcontracts, and subgrants.

Capital Outlay (objects 6000–6999), which includes expenditures for items such as the acquisition of land, improvements to sites, construction or purchase of new buildings, books and media for new schools, major expansions of school libraries, and capitalized equipment.

Other Outgo (objects 7000–7499) and Other Financing Uses (objects 7600–7699), which include items such as tuition, excess cost payments, pass-through funds, transfers out, debt service, and transfers between funds.

Since these costs are excluded from the determination of the indirect cost rate, it is not appropriate to include them in the pool of eligible program expenditures on which to charge indirect costs. (See CSAM Procedure 330 for further details on these categories of expenditures).

6. Is equipment, especially personal computers, considered capital outlay?

If the per unit cost of the personal computer exceeds the LEA's capitalization threshold, it is accounted for as capital outlay; if the per unit cost is below the capitalization threshold, it is considered materials and supplies, not capital outlay.

In general, there are certain criteria that must be met before equipment is considered to be capital outlay. CSAM Procedure 770 lists these criteria, such as whether the item has a normal service life of more than one year, the item is usually repaired rather than replaced, the cost to inventory the item is only a small percentage of the purchase price, and the item's per unit purchase price exceeds the LEA's capitalization threshold. CSAM recommends an equipment capitalization threshold of at least \$5,000, but this may vary by LEA. Procedure 770 also includes guidance on capitalizing groups of items acquired at the same time that do not meet the threshold for capitalization individually.

Equipment that costs more than the inventory threshold (typically \$500), but less than the capitalization threshold, is not considered capital outlay and is accounted for as noncapitalized equipment using Object 4400.

7. How is an indirect cost rate calculated?

The CDE has been granted authority by the ED to review and approve indirect cost rates for California LEAs (county offices of education, school districts, joint powers agencies, and charter schools).

Preliminary LEA indirect cost rates are calculated in the CDE's standardized account code structure (SACS) software using an indirect cost rate work sheet (Form ICR). To calculate the rate SACS Form ICR divides an LEA's general administration costs (the numerator of the calculation) by its operating costs (the denominator). An adjustment is also made for the difference between the rate approved for use in a year and the amount of indirect costs actually expended. (See CSAM Procedure 915 for further information on the indirect cost rate calculation).

LEAs annually submit Form ICR to the CDE along with their year-end financial reports. Once all LEA year-end financial data have been collected and reviewed by the CDE, a listing of approved indirect cost rates is posted.

8. How do I know what rate to use in what year?

The approved listing of indirect cost rates indicates in what fiscal year the rates are to be used. Data submitted for a particular fiscal year produce indirect cost rates that are used in the second

subsequent fiscal year (e.g., 2009–10 data produce indirect cost rates that are used in 2011–12).

The rate should be used in the fiscal year the funds are expended, which is not necessarily the same as the fiscal year the funds are appropriated, received, or encumbered. For instance, if money for a program is received in May 2010, which is part of fiscal year 2009–10, but the funds are not expended until fiscal year 2010–11, then the indirect cost rate approved for use in 2010–11 should be used when claiming indirect costs. This is because the indirect cost rate is meant to allow for recovery of costs in the fiscal year the expenditures are incurred, not the year the money may have become available.

9. What rate do I use for projects that cover more than one year?

If more than one fiscal year is involved in a project, the indirect cost rate used to recover indirect costs should change as the fiscal year changes. For instance, using an 18-month program starting August 1, 2010, the indirect cost rate approved for use in fiscal year 2010–11 would be used for expenditures incurred August 1, 2010, through June 30, 2011, and a new indirect cost rate approved for use in fiscal year 2011–12 would be used for expenditures incurred from July 1, 2011, until January 31, 2012.

For programs that follow the federal fiscal year, October 1 to September 30, the rates are still applied using the LEA's fiscal year as the basis. For example, the approved rate for the initial fiscal year would be used for October 1 through June 30, and then the new approved rate would be used for the July 1 through September 30 time period.

10. What determines if indirect costs can be charged to a program?

In the absence of statutory or regulatory language that would prohibit claiming indirect costs (e.g., if the legislation is silent on the subject of indirect costs), then indirect costs can generally be charged. But, if the authorizing legislation says that funds must be spent solely on the item in question, then indirect costs cannot usually be claimed. For instance, if a program states that funds are specifically limited to instructional materials, then charging indirect costs would not be allowed. (Because the statutes and regulations vary by program, questions on whether indirect costs can be charged to a specific program should be directed to the CDE unit responsible for administering the program.)

11. Is there a cap or limit on the amount of indirect costs that can be charged?

An LEA may claim up to its approved indirect cost rate unless there is specific authority (legislation or regulation) to limit the rate. For instance, if program statutory or regulatory language limits indirect costs to 3 percent, and an LEA has an approved rate of 5.25 percent, only 3 percent can be charged to the program for indirect costs; if the LEA had an approved rate of 2.75 percent, only 2.75 percent could be charged.

For caps associated with the food services programs, refer to question 17.

12. How do I use the indirect cost rate to recover/charge indirect costs?

If indirect costs are allowed, the indirect cost rate can be used to budget the maximum amount of indirect costs allowable for a program and then to claim the actual amount of indirect costs after the program expenditures have been made. It is important to remember that when recovering/charging indirect costs, the indirect cost rate is applied to the amount actually expended, not the total amount budgeted.

Example of budgeting for indirect costs: Assume an LEA's approved indirect cost rate is 8.00 percent and the grant amount is \$10,000. The LEA plans to spend the entire \$10,000 in the same fiscal year and does not expect to spend any of the \$10,000 on excluded costs (see question 5 for further information on excluded costs). Since the grant amount is for \$10,000, and indirect costs are part of the grant amount rather than in addition to it, you must back into a budgeted indirect cost amount that keeps the grant from exceeding \$10,000. To do this, divide \$10,000 by 1.08, which equals \$9,259.26. Then subtract \$9,259.26 from \$10,000, which equals \$740.74. The \$740.74 is the maximum amount the LEA could budget for indirect costs. (To test this, \$9,259.26 times 8.00 percent equals \$740.74, and \$9,259.26 plus \$740.74 equals \$10,000.)

Example of charging indirect costs: Assume an LEA's approved indirect cost rate is 8.00 percent and the grant amount is \$10,000. During the year, the LEA's actual grant expenditures totaled \$8,000, of which \$786 was for capital outlay (see question 5 for further information on capital outlay). The maximum amount that can be charged to the grant for indirect costs is \$577.12, which is \$7,214 (\$8,000 minus \$786) times 8.00 percent.

13. Does an LEA have to charge the entire amount of indirect costs allowed by its indirect cost rate?

An LEA may choose to claim less than the amount of indirect costs allowed by its indirect cost rate. Amounts not claimed under one award may not be shifted to another award, unless specifically authorized by legislation or regulation.

14. What about claiming indirect costs in contracts between LEAs and the CDE?

When indirect costs are allowed, LEAs should use their CDE-approved indirect cost rate as the basis for budgeting and claiming indirect cost reimbursements under contracts with the CDE. Contracts that cover more than one year should be structured to allow for adjustments for any rate(s) not yet known.

15. Do schools, including charter schools, have approved indirect cost rates?

Non-charter schools fall under the authority of their district; their expenditures are reported to the state as part of the district's General Fund and are used in the calculation of the district's indirect cost rate. This enables non-charter schools to use the indirect cost rate approved for their district.

Because of the unique circumstances surrounding charter schools, some are able to use the rate of their approving agency and some are not, depending on how their year-end expenditures were reported to the state. Please see our separate [charter school listing](#) for details on approved rates for charter schools.

16. Are there indirect cost rates for community colleges?

The CDE's federally approved indirect cost plan only covers kindergarten through grade twelve (K–12) educational programs. Questions about indirect cost rates for community colleges should be directed to the Chancellor's Office at 916-445-8752.

17. Are there statewide indirect cost rates?

In compliance with *Education Code* sections 38101(c), the CDE annually calculates a statewide average rate for use by LEAs to recover indirect costs from food service programs. The food service programs limit indirect costs to the lesser of the LEA's approved rate or the statewide average rate.

The CDE calculates the statewide average rate by totaling the expenditures of elementary, high, unified, and common administration districts, thereby creating one statewide indirect cost pool and one statewide direct/direct support cost pool. The rest of the calculation is done the same as for individual LEAs, as if the statewide expenditures from all LEAs were a single LEA. For the latest statewide rate, please see our [statewide rates listing](#).

18. Can entities other than LEAs get an indirect cost rate?

The CDE may assign indirect cost rates to non-LEAs that receive funding from the CDE as long as the non-LEA receives little or no funding directly from any federal agency. (A non-LEA that receives funding directly from a federal agency would apply to that agency for a rate.) Examples of non-LEAs covered by this include private schools, consortia, and nonprofit entities (other than charter schools).

Non-LEAs requesting an indirect cost rate from the CDE should contact the Office of Financial Accountability and Information Services by e-mail or by phone as listed in the Questions section of this page.

Questions: Financial Accountability & Information Services | sacsinfo@cde.ca.gov | 916-322-1770

Last Reviewed: Friday, April 17, 2015
