



EXECUTIVE OFFICE OF THE PRESIDENT  
OFFICE OF MANAGEMENT AND BUDGET  
WASHINGTON, D.C. 20503

THE DIRECTOR

May 11, 2009

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MEMORANDUM FOR THE HEADS OF DEPARTMENTS AND AGENCIES

FROM: Peter R. Orszag  
Director

SUBJECT: Payments to State Grantees for Administrative Costs of Recovery Act Activities

The Administration remains committed to effective implementation of the American Recovery and Reinvestment Act (“Recovery Act”). A majority of Recovery Act dollars are disbursed by the States, who thus play a central role in the prudent, timely, and transparent expenditure of Recovery funds. It is therefore critical that State governments quickly and effectively build the necessary administrative capacities to meet their reporting and other responsibilities under the Act. OMB has been working closely with Federal agencies and State governments to identify potential barriers to State implementation efforts and identify solutions that will enable successful outcomes.

The Recovery Act implementation officials of many States have asked OMB to assess the process by which States recover administrative costs associated with Federal grant programs. In particular, unlike other grant recipients such as colleges and universities, States do not generally recover central administrative costs up-front, but instead are reimbursed for such expenses after the fact. This process can have the unintended consequence of preventing State governments from obtaining the necessary resources to build quickly administrative capacities to meet the important new oversight, reporting and audit requirements of the Recovery Act.

This memorandum addresses this issue by clarifying and encouraging States to utilize existing flexibilities to recover administrative costs related to carrying out Recovery Act programs and activities in a more timely manner.

Background

Central administrative costs incurred by State recipients in the management and administration of Recovery Act programs are allowable costs under the current guidance of OMB Circular A-87, Cost Principles for State, Local and Indian Tribal Governments.<sup>1</sup> Generally, these costs are recovered as indirect costs to the programs. The methodology used to reimburse State recipients for central administrative costs is captured in the indirect cost rates provided for in OMB Circular A-87.

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<sup>1</sup> OMB also issues guidance on administrative cost principals to non-profit organizations (Circular A-122) and colleges and universities (Circular A-21). These Circulars will not be amended for Recovery Act purposes.

Under the provisions of OMB Circular A-87, States can recoup Recovery Act administrative costs through the State-wide Cost Allocation Plan (SWCAP), which is submitted to the Department of Health and Human Services (HHS) annually for review and approval. The costs can either be included as “centralized services” costs (commonly known as “Section I costs”) or as “billed services” costs (commonly known as “Section II costs”). These costs can be included in the SWCAP as an addendum plan pertaining only to Recovery Act programs and activities, thus providing transparency to the total amount of Recovery Act administrative costs and its allocation to the programs. Specific guidance for developing the SWCAP is provided in OMB Circular A-87, Attachment C, *State/Local Wide Central Cost Allocation Plans* and HHS’s document - *Cost Principles and Procedures for Developing Cost Allocation Plans and Indirect Cost Rates for Agreements with the Federal Government (ASMB C-10)* [<http://rates.psc.gov/fms/dca/asmb%20c-10.pdf>].

### Alternatives for Administrative Cost Reimbursement

*Alternative 1, Use of Estimated Costs for Centralized Services.* As centralized services costs, instead of using the actual costs for calculation, a State is authorized to use *budgeted or estimated* costs for the Recovery Act in the submission of the SWCAP. The budgeted or estimated cost amount should not be in excess of 0.5 percent of total Recovery Act funds received by the State. The SWCAP must include the following for the Recovery Act central services: a brief description of the service, an identification of the unit rendering the service and the operating agencies receiving the service, the basis for the budgeted or estimated amounts, the types of expenses in the service, the allocation methods of the service costs to benefitted agencies and a summary schedule showing the allocation of each service to the specific benefitted agencies. Once the SWCAP is approved by HHS, the amounts can be included in the State agencies’ indirect cost rates and billed to Recovery Act programs. Reconciliation between actual costs and claimed costs will be made in the subsequent year review of the SWCAP, with the difference recouped through carry-forward adjustments.

*Alternative 2, Billed Services.* As “billed services” costs, a State may submit the methodology for identifying, recording and charging administrative costs to Recovery Act grants to HHS for review. The SWCAP must include the following: a brief description of the service, the budgeted or estimated expenses statement, a description of the procedures (methodology) used to charge the costs of each service to users (including how billing rates are determined), a schedule of developed rates and an explanation on how variances between actual and billed rates will be handled. Once approved, the methodology may be used to charge administrative costs to State agencies that would recover these costs through billing of the Recovery Act programs (e.g., on a monthly, biweekly or weekly basis). The administrative costs billed to Recovery Act programs should not be in excess of 0.5 percent of total Recovery Act funds received by the State. A reconciliation of expenses and revenue statement would be submitted with the annual SWCAP.

Both options, allowed currently under the provisions of OMB Circular A-87, provide flexibility for States to recoup the administrative costs related to Recovery Act activities more quickly than would be permitted under the traditional SWCAP process. This should enable States to obtain the resources necessary for enhancing their administrative capacity to meet Recovery Act responsibilities.

Please contact the Office of Federal Financial Management within OMB at 202-395-3993 or [recovery@omb.eop.gov](mailto:recovery@omb.eop.gov) for additional information on this guidance. Please contact the Division of Cost Allocation's cognizant field offices, Department of Health and Human Services, to discuss the preparation and submission processes. States will be able to locate HHS Field Office assignments and Q&A on [www.rates.hhs.gov](http://www.rates.hhs.gov).