Further Discussion on Proper Grant Costs:

Let’s look at the definition of Grant Costs in detail. Remember, you as the accountant are IMPORTANT to internal control. You are supposed to know all of this AND are to alert management or the Board if anything is happening that is not right and is not being corrected. You are IMPORTANT!!!!

#1 REASONABLE. What is Reasonable?  Is this a reasonable purchase? It may say hot dog on the receipt, but you, the accountant, need to make sure it truly is a reasonable purchase.

If you look at your Federal OMB Requirements on page 78640 (really, page 78640), you will see what they call reasonable. Please take a moment to read it.

I have seen pets charged as security, vacations charged as research, commuting charged as travel, Art charged as supplies and so on. So, I ask that you define reasonable by asking, “ if the grantor were to visit you (and they very well may), would he or she agree with what you consider reasonable?” My recommendation here is use good judgment because if the government or private auditor disagrees on an expense, you can’t get the money back, it’s spent.

#2 DIRECT COSTS AND INDIRECT COSTS: Costs that fulfill the grant’s purpose in some way.

**Directly related** means that the cost is 100% for the grant. There are 2 ways to determine directly related costs:

1. Source document is 100% for a grant or specific grants. For these, the amounts and benefits are clearly documented as to what grants received the benefit and should be charged. This can be 1 invoice for 1 grant or 1 invoice for more than 1 grant. For instance, you purchase 5 computers on 1 invoice; 3 for Grant A and 2 for Grant B. These are still direct costs because you can show the direct correlation of the cost to the grant.
2. Prorated Source documents for 2 or more grants. These costs are allowable direct costs that can be identified to two or more grants and are prorated using an appropriate method particular to the cost being prorated. For example, Grants A, B and C all use one rental building. You would charge the rent of the building to each of the 3 grants based on the square footage each uses exclusively. Thus, this is a prorated cost that directly benefits only these 3 grants.

**Indirectly allocable** means that the costs cannot be readily identified with a particular grant or funding source. These costs benefit all programs or so many that they cannot be broken out on a reasonable pro-rata basis. For instance, administration or organization wide facility costs. These costs can be allocated to each grant using a basis that results in an equitable distribution.

The key here is to not just charge these costs to grants as direct costs. This is a red flag to any auditor. For instance, if all of the Organization’s admin rent is charged to 3 grants and none of it is charged anywhere else, this could be an unallowable cost, even if the grant has enough in its budget to pay all the rent. This happens a lot. I also see this with the Accounting staff or Executive Director salary and related payroll expenses. They are charged to several (fat) grants while the lean grants don’t have any of this charged.

We will go over proper allocation a little later as it’s a separate section in our Grant Accounting seminar.

#3 CONFORM TO LIMITATIONS: Grants limit certain costs. Therefore, it would be prudent to review each grant to determine any limitations that apply. For instance, some grants require “American Made” products where possible. Some grants prohibit purchasing medicine. Other grants do not allow deviations from approved budgets and so on. Each grant could have some limiting provisions that you need to know about. When you note a limitation, you should note it on your grant info sheet under grant compliance requirements. We recommend the following procedures:

1. Read the grant.
2. Document in the grant file the following:
	1. Budget – The budget is also a spending guideline. Most grants don’t allow a more than 10% deviation from the approved budget without approval.
	2. Specific Exceptions – Any and costs prohibited in the grant. Such as no alcoholic beverages, no travel, no admin, no fundraising, no medical treatment, etc.
	3. Specific Inclusions – Any spending requirements. Such as 10% will be used for Hilo clients or 10% will be used for Native Hawaiians or purchase a vehicle, etc. Or purchases should be made after accepting a minimum of three vendor bids.
3. Also worth noting as specific limitations will be any regulations applying to the grant by reference. All Federal grants have the OMB Circulars that apply as do many State grants. In addition, many agencies, such as HUD or NIH or State Dept. of Housing, have their own regulations and requirements that are to be adhered to. Thus, you should note these and get them and read them. The HUD guidelines alone are massive. You can take classes and get HUD certified. There may be other similar training classes for other Government agencies.

The overall point here is to know what additional limitations, exclusions or inclusions each grant may require. Then document them and plan to adhere to them during the year. I would also make sure the program decision makers know what they are as well.

#4 CONSISTENT TREATMENT: Expenses charged to grants need to be recorded consistently with all other expenses. The main point here is that you treat all the grants the same in your accounting. If you use square footage to allocate rent for the Federal grants, you should do the same for all the funding sources and you need to use the same square footage rate. Of course this is to avoid having different accounting treatment that unfairly charges one grant more than another.

A good rental allocation method would NOT be to allocate $3 per foot to the Federal grants, $2 per foot to the State grants, and $0 per square foot to admin and fundraising. This is not consistent treatment.

#5 GAAP which is Generally Accepted Accounting Principals. GAAP is specifically noted in the Federal OMB Requirements, which applies to all Federal funds. Thus, you should not use Cash basis of accounting or modified Cash basis. Accrual is the way to go.

One Exception to GAAP is when the grant allows a cost that is not a GAAP expense. The most common is a fixed asset purchased with Grant funds. For instance, if the Grant allows for the purchase of a bus and the budget shows the full cost of the bus, then the Bus purchase is a grant cost. However, you cannot show this as an expense on your final GAAP financial statements.

Therefore, you need to do Carbo Grant Accounting to show it as a grant expense and an expense at the same time. The Bus cost is an expense on the grant accounting class. In the General Class, a credit to the Bus expense is posted with the debit to fixed assets. Thus total P&L is correct, the asset is on the balance sheet and depreciation is charged to the General class and NOT allocated.

Note: If the asset is to revert to the grantor if not used by the Organization, we still recommend you capitalize it and show the restriction on it in the footnotes or on the face of the balance sheet. The reason for this is the intended use of the asset will fully be by the Organization and the reversion to the grantor would be an unlikely event.

#6 CHARGED TO ONLY 1 GRANT:  A grant cost can only be charged to 1 grant or funding source. Not many things give government auditors more pleasure than “catching” someone charging the same cost to two or more grants. I suspect that “double dipping”, as this is referred to, is high on the risk list for auditors in general.

Thus, you should have a good internal control system that prevents “double dipping.” Some ways to prevent double dipping are:

1. Coding each invoice or source document with the grant/grants it’s charged to.
2. Marking invoices and source documents as “paid” or “entered” when coded in accounting system.
3. Double checking journal entries to make sure any added costs to one grant are taken away from another.
4. Making sure allocations of indirect costs do not include any direct costs.
5. This can be done with an indirect cost class.
6. It’s good practice to charge invoices to an expense account, not a clearing account.

Also, many Federal grants, some State and private grants have matching requirements. A matching requirement is to have some other source of revenue paying for costs that contribute to the grant’s fulfillment. For instance, many Fed Department of Health and Human Services grants require $1 of matching costs for every $5 of Federal grant costs.

The Federal grant requirement is that you can not use another Federal grant to provide the matching costs, unless specifically allowed in writing. Thus, if you have DHS grant #1 that pays the $5, you can not have HUD grant #2 pay the $1 matching. Usually matching requirements are spelled out in the grants themselves.

#7 ADEQUATE DOCUMENTATION: I went to a non-profit conference in Portland, Oregon and the Fed auditor said the #1 problem encountered in doing audits and reviewing the audits of CPAs is the lack of payroll documentation for payroll charged to federal grants. It is possible that legitimate costs paid could be disallowed if the Organization can’t prove after the fact that the costs were really for the grant. Thus, documentation is crucial.

For the benefit of anyone needing to reference the grant related records, it’s a good idea to notate on your disbursement documentation, the accounts affected, grant classes, and to have the appropriate dated authorization or reference to the budget. And as previously mentioned, these should all agree to your accounting entries and be kept in the grant file. For travel and meals and other items where the business purpose is not readily apparent from the documentation, you should note on the documents the business purpose, people included and any other information that shows how the cost fulfills grant purposes.

FYI The meat and potatoes of Grant Costs is in the Federal OMB Requirements in Subpart E which starts on page 78639. This section also allows you to show your Board and E.D. what is allowable so that it (the Fed OMB Requirements) are the “bad guy” and not you the awesome accountant. You are just the messenger.