

U.S. Department of Housing and Urban Development  
Community Planning and Development



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Special Attention of:

**Notice:** CPD 13-07

All CPD Division Directors

All CDBG Grantees

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**SUBJECT:** Allocating Staff Costs between Program Administration Costs vs. Activity Delivery Costs in the Community Development Block Grant (CDBG) Program for Entitlement Grantees, Insular Areas, Non-Entitlement Counties in Hawaii, and Disaster Recovery Grantees

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## **I. INTRODUCTION AND PURPOSE**

There has been much confusion when determining whether a staff cost should be allocable as a program administrative cost or an activity delivery cost, as well as confusion over the treatment of direct or indirect costs associated with these two cost categories.

This Notice provides guidance on the allocation of staff costs for the CDBG program between two cost categories: (1) general program administrative costs, as related to overall program planning and CDBG grant administration; and (2) activity delivery costs, as related to implementing and carrying out specific CDBG-eligible activities.

HUD recognizes that the existing use of “administration” throughout its regulations can cause confusion. To clarify, the Office of Block Grant Assistance will use the term PACs for Program Administrative Costs and ADCs for Activity Delivery Costs, in order to differentiate between the two.

The Office of Management and Budget (OMB) establishes principles to maintain a uniform approach for determining costs and promoting effective program delivery and efficiency. The most applicable sections to the CDBG program are: OMB Circular A-87, which has been relocated to 2 CFR Part 225, and contains the Cost Principles for State, Local, and Indian Tribe Governments, and OMB Circular A-122, which has been relocated to 2 CFR Part 230, and contains the Cost Principles for Nonprofit Organizations. The basic guidelines address the following aspects of costs: the factors of cost allowability, cost reasonableness, allocable costs, applicable credits, and the composition of costs as either direct or indirect. These principles also provide guidance for allocating allowable costs to program administration costs or activities with final cost objectives (see Appendix C for definition of final cost objectives) to activity delivery costs.

The Insular Areas (Guam, Virgin Islands, American Samoa, Trust Territory of the Pacific Islands, and the Northern Mariana Islands) and Nonentitlement Areas in Hawaii follow the Part 570 regulations for entitlement communities regarding PACs and ADCs. The treatment of these costs for the State CDBG program is not addressed in this guidance.

## **II. BACKGROUND**

*Program administration costs (PACs).* The statutory provision regarding the eligible use of CDBG funds to pay PACs is section 105(a)(13) of the Housing and Community Development of 1974, as amended (the HCDA). The general program administration regulations are codified at 24 CFR 570.205 and 570.206. Costs attributable to program administration are limited in that not more than 20 percent of the annual grant, and the estimated amount of program income to be received during the grantee’s current program year, can be obligated by entitlement grantees, Insular Areas, and Nonentitlement Counties in Hawaii for such costs. The 20 percent limitation is not contained in the HCDA, but has been included in annual appropriations acts for the CDBG program since 1978. The limitation on program administration costs is codified at 24 CFR 570.200(g). Examples of program administration costs allocable to the CDBG program include the following:

1. Salaries of executive officers and staff with general program oversight responsibilities;
2. Leased office space for staff employed in carrying out the CDBG program;
3. Staff time spent for the development of general CDBG program policies and procedures, such as the monitoring of overall program performance;
4. Staff time spent for the development of the Consolidated Plan/Action Plan and Consolidated Annual Performance and Evaluation Report (CAPER); and
5. Administrative services performed under third-party contracts, such as legal, accounting, and auditing services or development of the Consolidated Plan.

As noted above, under the authority of 24 CFR 570.206, CDBG funds may be used to pay staff costs for persons responsible for general CDBG program administration as a whole. These general PACs cover such positions as a community development director, urban planner generalists, and general administrative and clerical staff. In addition, staff costs associated with compliance oversight and monitoring of a grantee's subrecipients would generally fall under the program administration cost category as well unless such costs may be allocated to a final cost objective.

*Activity delivery costs (ADCs).* ADCs are those allowable costs incurred for implementing and carrying out eligible CDBG activities. All ADCs are allocable to a CDBG activity, including direct and indirect costs integral to the delivery of the final CDBG-assisted activity. CDBG expenditures for activity delivery costs are not governed by 24 CFR 570.205 and 570.206.

To recognize the difference between ADCs and PACs, 24 CFR 570.206 notes that "staff and overhead costs directly related to carrying out activities [are] eligible under 570.201 through 570.204, since those costs are eligible as part of such activities." In addition, 24 CFR 570.205(a)(4)(iii) and (iv) state that "...engineering and design costs related to a specific activity... are eligible as part of the cost of such activity under 570.201-570.204." Examples of ADCs allocable to CDBG activities include the following:

1. Compensation of employees for the time devoted to the performance of implementing and carrying out a specific eligible CDBG activity, such as carrying out as a public service or implementing an ongoing housing rehabilitation program;
2. Cost of materials acquired, consumed, or expended by staff in carrying out a specific eligible CDBG activity, such as the paper for housing rehabilitation program applications or uniforms for code enforcement staff working in eligible areas; and
3. Travel costs incurred specifically for carrying out eligible activities, such as visits made to the job site of a housing rehabilitation activity to ensure legitimate progress payments.

*Direct and Indirect Costs.* All costs are either direct or indirect under every accounting system. A cost may be direct with respect to some specific service or function, but indirect with respect to the Federal award or other final cost objective. General standards and guidelines for determining direct and indirect costs charged to Federal awards are provided at Appendix A to 2 CFR Part 225.

According to Appendix C, Section E, direct costs are those that can be identified specifically with a particular final cost objective. Typical direct costs chargeable to Federal awards are compensation of employees for the time devoted and identified specifically to the performance of those awards; the cost of materials acquired, consumed, or expended specifically for the purpose of those awards; equipment and other approved capital expenditures; and travel expenses incurred specifically to carry out the award. In addition, any direct cost of a minor amount may be treated as an indirect cost for reasons of practicality where such accounting treatment for that item of cost is consistently applied to all cost objectives.

According to Section F of Appendix A, general indirect costs are those incurred for a common or joint purpose benefiting more than one cost objective, and not readily assignable to the cost objectives specifically benefitted, without effort disproportionate to the results achieved. The term "indirect costs," as used herein, applies to costs of this type originating in the grantee department, as well as those incurred by other departments in supplying goods, services, and facilities. To facilitate equitable distribution of indirect expenses to the cost objectives served, it may be necessary to establish a number of pools of indirect costs within a governmental unit department or in other agencies providing services to a governmental unit department. Indirect cost pools should be distributed to benefitted cost objectives on bases that will produce an equitable result in consideration of relative benefits derived.

### **III. ALLOCATION OF STAFF COSTS**

#### **A. Program Administration Costs (PACs)**

The allocation of staff-time costs and overhead charges to general program administration is eligible under 24 CFR 570.205 and 570.206. These provisions allow "reasonable administrative costs and carrying charges related to the planning and execution of community development activities assisted in whole or in part [with CDBG funds]." As set forth at 24 CFR 570.200(g), HUD will find a grantee in compliance with this requirement if the grantee limits the amount of CDBG funds *obligated* for planning plus administration during each program year to an amount not greater than 20 percent of the sum of its entitlement grant made for that program year plus the estimated amount of program income to be received by the grantee and its subrecipients during that same program year.

##### **1. The National Objective and Proportional Costs**

The HCDA requires that CDBG expenditures be made for eligible activities that result in meeting one of three national objectives: (1) provides benefit principally to persons of low and moderate income (LMI); (2) aids in the prevention or elimination of slums or blight; or (3) meet a need having a particular urgency that the grantee is unable to finance on its own. However, general PACs are not required to meet a specific CDBG national objective because such costs are generally made in support of other CDBG-eligible activities that meet a national objective. Thus, PACs are *not* calculated under the 70 percent overall LMI benefit requirement at 24 CFR 570.200(a)(3)(i).

Where an individual performs general administration functions and implements specific eligible CDBG activities under 24 CFR 570.201-204, the grantee may elect to charge *all* of such staff costs to the program administration category, or *only a portion* of such costs to program administration, with the balance of CDBG-eligible costs allocable to the activity as ADCs. It is important that the grantee ensure that only ADC-eligible costs are charged to this category. However, PACs may not be charged as ADCs. It is also important that the treatment of dividing allocable costs between PACs and ADCs is consistently applied and supported by staff timesheet documentation relative to specific eligible activities.

## **2. Urban County and Subrecipient Administrative Costs**

An urban county entitlement grantee must be especially cognizant of allocating staff costs for general administration and oversight of its CDBG program. To carry out any eligible CDBG activity, the county can use its own staff, the staff of a unit of general local government (UGLG), a subrecipient's staff [as defined in 24 CFR 570.500(c)], or contractor's staff [as procured in compliance with 24 CFR 570.85.36]. An urban county has a unique relationship with an UGLG, as it is required to impose upon a participating UGLG the same requirements that apply to a subrecipient [See 24 CFR 570.501(b) and 570.503 requirements]. Persons responsible for administering the general CDBG program as a whole either at the county level or the UGLG level would incur staff costs allocable to the general program administration costs category [24 CFR 570.206] and thus be subject to the 20 percent cap. (HUD has issued previous guidance on subrecipient agreements and grantee management in "*Managing CDBG: a Guidebook for Entitlement Grantees on Subrecipient Oversight*," March 2005.)

UGLGs are generally awarded CDBG funds by the urban county and treated as subrecipients to carry out eligible activities within the county's boundaries. The county uses its staff to administer UGLG cooperation agreements and monitor UGLG performance as appropriate. Notwithstanding, a question may arise regarding the salary of a person that works for the UGLG that is carrying out a series of eligible activities, as there may be instances in which the UGLG staff generally administer the contract and contract performance, and carry out a portion of the associated ADCs for a project with a final cost objective. In such instances, the UGLG's staff time shall be prorated and allocated to each cost category (PACs and ADCs) accordingly. Care is warranted, as it is the urban county that is responsible for ensuring that staff costs incurred by the UGLG are allocated appropriately as PACs or ADCs as described in this Notice. County staff may incur both ADCs and PACs in some cases. An example is conducting or attending job walks, bid openings, and pre-construction conferences for construction projects. If the urban county is overseeing and reviewing preconstruction activities for a participating UGLG, the cost would be classified as a PAC. However, if the county was directly managing pre-construction activity rather than the UGLG, the cost would be classified as an ADC.

Grantees are reminded to monitor activities carried out by their staff and their subrecipients to ensure that general administrative costs are not inappropriately charged as activity delivery costs as a means to avoid the 20 percent program administration cap. Moreover, all costs must be allocable as either direct or indirect costs according to 2 CFR 225.

### 3. Allocating other CPD programs' administrative costs to CDBG

Grantees may charge other formula program [e.g., HOME, ESG, or HOPWA] PACs to the CDBG program in certain circumstances, subject to the limitations below. However, this is not permitted with CDBG Disaster Recovery funds. PACs are allocable to other formula CDBG programs in proportion to the amount of time staff spend working on such programs, or with regard to managing activities in support of other programs, such as is the case with the use of CDBG to pay general program administration costs for the HOME program [24 CFR 570.206(i)(2)]. However, it is critical to note that where such costs are collectively treated as program administration because they are subject to the CDBG program's overall 20 percent cap on PACs.

Grantees must maintain adequate records and documentation in support of all costs, as set forth in the following sections of the regulations: 24 CFR 570.502 and 570.506; and Part 85.20, standards for financial management systems. Additionally, the grantee's records should clearly show there is a consistent treatment of like costs under similar circumstances.

- a. *HOME and EZ/EC Costs.* Section 105(a)(13) of the HCDA and 24 CFR 570.206(i) provide that CDBG funds may be used to pay costs for carrying out the overall administration of a *federally* designated Empowerment Zone (EZ) or Enterprise Community (EC), and the Affordable Housing Program (HOME) under 24 CFR Part 92 and 24 CFR 570.206. Renewal Communities (RCs) are not included as eligible communities under this statutory and regulatory provision. CDBG funds may be used to pay a combination of PACs for these EZs, ECs, and the HOME program; however as noted earlier, the combined costs for using CDBG in this manner is subject to CDBG's overall 20 percent cap. To illustrate, in a current program year, if a grantee decides to obligate 10 percent of its program administration budget for the HOME program, then it must limit its obligations for its CDBG program administration costs to 10 percent in the same program year.

Section 105(a)(20) of the HCDA states that CDBG funds may be used to pay for housing services associated with projects assisted under the HOME program. This CDBG eligible activity was promulgated under 24 CFR 570.201(k) in the Entitlement program. Hence, while HOME program administration costs remained eligible under Section 105(a)(13) of the HCDA and 24 CFR 570.206(i) in the Entitlement program, HOME ADCs became eligible under 24 CFR 570.201(k). (See section III B. of this Notice for further discussion of ADCs under the HOME program.)

- b. *ESG, SHP, HOPWA Costs.* As a general rule, neither the statute nor the regulations provide for the use of CDBG funds to pay PACs *solely* for the administration of the following CPD programs: Emergency Solutions Grant (ESG) program, the Supportive Housing Program (SHP) program, RCs, or the Housing Opportunities for Persons with AIDS (HOPWA) program. For example, a staff person in a general administrative position that works only for the ESG program may not be paid with CDBG funds for their time spent on the ESG program.

Notwithstanding, there are circumstances where CDBG funds may be used for staff administration costs associated with eligible ESG, SHP, or HOPWA activities (such as homeless services, health screening, or job training). CDBG funds may be used to pay PACs attributable to any of these programs if the activities carried out are otherwise CDBG eligible and meet all CDBG requirements (e.g., eligibility, national objective compliance, and environmental review requirements). For example, when a staff person spends most of his/her time administering the CDBG program, and a small part of their time carrying out general administrative functions for the ESG program, the *only* administrative staff time allocable to the CDBG program is that time spent on administering the CDBG program and carrying out CDBG-eligible ESG activities.

- c. *Consolidated Plan and Annual Action Plan Costs.* Another circumstance where costs are eligible as CDBG PACs is when the grantee is preparing its Consolidated Plan and/or annual Action Plan [24 CFR Part 91]. During this program administration exercise, staff costs associated with all of the components of completing the Consolidated Plan to be assisted by any or all four CPD formula grant programs (CDBG, HOME, ESG, and HOPWA) to be identified in the Consolidated Plan and annual Action Plan may be allocated to the CDBG program as PACs. [See 24 CFR 570.205 and .206.]

#### **4. Other types of eligible administrative staff costs**

- a. *Administrative expenses to facilitate housing.* Often grantees ask whether or not they can charge planning and financial administrative costs for housing to the CDBG program under 24 CFR 570.206(g). However, 24 CFR 570.206(g) refers to housing identified in a recipient's Housing Assistance Plan (the HAP), which is no longer in use and was replaced by the Consolidated Plan. Inasmuch as the Consolidated Plan includes non-housing activities, and is not exclusively limited to low- and moderate-income persons, the Department has determined that 24 CFR 570.206(g) cannot be read to substitute costs related to the Consolidated Plan for costs formerly eligible in connection with the HAP. However, if a specific activity is construed to involve a HAP-type implementing activity, the Department is willing to consider a waiver of this section of the regulations to permit the expenditure of CDBG funds for statutorily permissible planning and administrative expenses designed to facilitate housing development. The Assistant Secretary for Community Planning and Development (CPD) will make the final written determination with regard to a CPD program waiver.
- b. *Activities to further fair housing.* The costs associated with the development of an analysis of impediments to fair housing and development and implementing local initiatives to affirmatively further fair housing may be allocated to the Consolidated Planning activity as program administration costs. Alternatively, certain fair housing activity costs, such as housing counseling, may be CDBG-eligible and allocable as activity delivery costs.

## 5. Ineligible Costs

*General administrative affairs of government.* Per Section 102(a)(21) of the HCDA and 24 CFR 570.207(a)(1), buildings or portions thereof used for the general conduct of government cannot be assisted with CDBG funds. HUD's Office of General Counsel has stated the "general administrative affairs of government" consists of overall departmental and program management and operation functions, including executive, management, and clerical functions; and purely administration function such as personnel, legal, and accounting departments.

## 6. Identifying A Final Cost Objective

In the initial stages of creating a project, there may be general administrative costs allocable as PACs; however, as the project progresses, such costs may qualify as implementing ADCs and linked to the final cost objective. This is consistent with treating costs that support the final cost objective. For example, costs identified as PACs at the onset of a project, such as preparing a request for proposal, reviewing bid proposals, and preparing contract documents, may be administrative in nature, but if such costs are part of the implementation of the activity and can be identified with a final cost objective, then allocating such staff costs as ADCs is the appropriate cost treatment.

On the other hand, a grantee must be aware of the risk associated with initiating a project that does not materialize or reach fruition and, therefore, does not meet a CDBG national objective or a final cost objective. In such cases, the incomplete activity will most likely be determined ineligible and the staff costs disallowed or possibly considered general administrative costs. When such costs are assigned as PACs, the grantee's obligations may exceed the 20 percent program administration cost limitation. Accordingly, HUD may advise the grantee to repay its CDBG program line-of-credit with non-federal funds for the amount in excess of the 20 percent cap.

Grantees must maintain adequate records and documentation in support of all costs, as set forth in 24 CFR 570.502 and 570.506, and Part 85.20, standards for financial management systems. Additionally, the grantee's records should clearly show there is a consistent treatment of like costs under similar circumstances.

There has been confusion in allocating staff costs associated with complex activities designed to operate as programs. Such activities include housing rehabilitation programs, economic development loan programs, microenterprise development programs, and homebuyer assistance programs. To be clear, housing rehabilitation administration is the only activity that has a separate IDIS matrix code that allows for the allocation of administrative costs as ADCs. This category is used to charge housing rehabilitation administration costs for all CDBG-assisted housing rehabilitation and housing rehabilitation carried out using other funding sources that meet all CDBG program requirements. For other program-type activities, general program administrative costs are treated as PACs and subject to the 20 percent cap. For this reason, grantees operating programs must use care in identifying which costs can be consistently treated as ADCs (i.e., part of delivering a final cost objective) versus those costs that are identified as general administration costs. See Table 1 below regarding the allocation of costs and HUD's

Integrated Disbursement and Information System (IDIS), Matrix Codes. The table shows eligible activities, the proper cost category, statutory and regulatory references, and the IDIS matrix codes.

Table 1 - Allocable PACs and ADCs for eligible activity program-type costs

Program	Cost Categories (PACs or ADCs)	HCD Statute	Regulation	IDIS Matrix Code
Rehabilitation - Admin. Services	ADCs	105(a)(1)	570.202(b)(9)	14H - <u>Not</u> Subject to the 20% cap, but included as ADCs
Types of Eligible Buildings and Improvements	ADCs	105(a)(1)	570.202(a)(1-4)	14A
HOME - Admin. Costs	PACs	105(a)(13)	570.206(i)(2)	21H - All Non-ADCs subject to 20% CDBG Cap
HOME Services Eligible under CDBG	ADCs	105(a)(20)	570.201(k)	14J
Special Economic Development Admin.	PACs	105(a)(13)	570.206	20 and 21A - All Non-ADCs subject to 20% CDBG Cap
Special ED Activity Delivery & Services	ADCs	105(a)(15)	570.203(a), (b) and (c)	17A, 18A, 18B
Microenterprise Program - Admin. Costs	PACs	105(a)(13)	570.206	20 - All Non-ADCs subject to 20% CDBG Cap
Microenterprise Delivery Costs for Activities	ADCs	105(a)(23)	570.201(o)	18C
Homeownership Assistance Program Admin.	PAC	105(a)(25)	570.201(n)	20 - All Non-ADCs subject to 20% CDBG Cap
Homeownership Assistance Delivery Costs	ADCs	105(a)(23)	570.201(n)	13

PACs = Program Administration Costs

ADCs = Activity Delivery Costs

Table 2 below presents the IDIS matrix codes that may be used when charging costs to program administration.

Table 2 – IDIS Matrix Codes for Program Administration Costs

<u>Matrix Code</u>	<u>Eligible Activity</u>	<u>Regulatory Citation</u>
20	Planning	24 CFR 570.205
21	General Program Administration	24 CFR 570.206
21B	Indirect Costs	24 CFR 570.206
21D	Fair Housing Activities	24 CFR 570.206
21E	Submission of Applications for Federal Programs	24 CFR 570.206

## B. Activity Delivery Costs (ADCs)

### 1. General

Activity delivery costs (ADCs) are those costs *not* subject to the 20 percent limitation for PACs. ADC staff costs are considered part of the costs for carrying out an eligible CDBG activity pursuant to 24 CFR 570.201 – 570.204. Accordingly they are treated as part of the total cost for delivering a final cost objective under the CDBG program. This is the only limiting requirement – that ADCs are incurred in order to implement and carry out specific CDBG-assisted activities. 24 CFR 570.205(a)(4)(iii) affirms this as it states, “...engineering and design costs related to a specific activity... are eligible as part of the cost of such activity under 570.201-570.204.”

At times the initial costs for an eligible CDBG activity may be treated as administrative costs; however, in the activity’s final accounting, it may be more appropriate to treat these costs as ADCs. Generally, for example, staff costs for performing environmental reviews or housing relocation work are considered part of the total ADCs associated with the underlying CDBG-assisted activity. At times, incurring up-front costs may appear PACs in nature, but upon completion of the activity these costs can re-allocated as ADCs. As an example, if staff time spent for preparing and issuing a request for proposals (RFP) for multifamily housing rehabilitation, reviewing and selecting bids, and preparing contract documents and notices to proceed can be identified as part of the final cost objective, then allocating these costs as ADCs is the appropriate cost treatment for those properties that proceed to completion and occupancy.

Notwithstanding, there is risk in allocating costs in this manner. Where an activity is not completed, or the activity does not meet a CDBG national objective, the up-front costs must be allocated as PACs because they cannot be associated with achieving a final cost objective. In such cases where this would result in obligations or expenditures exceeding a grantee’s 20 percent program administration cap, HUD may advise the grantee to repay its CDBG program for any amount above the cap with non-federal funds. In the above example, staff time spent reviewing proposals for multifamily housing rehabilitation projects that do not proceed to completion cannot be charged as ADCs, as there is no funded activity (and no final cost objective) to charge them to.

It is important to recognize that staff time allocable as ADCs represents the actual time spent on implementing and completing an eligible CDBG activity. For example, staff time for a housing rehabilitation specialist, whose duties are to make home inspections, prepare work write-ups, and inspect projects through completion, would be 100 percent allocable as rehabilitation activity delivery costs. However, circumstances may require that the project incurs other staff costs for personnel that spend less than 100 percent of their time working for the rehabilitation program. For example, a project may need a city engineer to approve, inspect, and sign off on integral structural improvement. Hence, the engineer’s staff-time can be prorated and allocable as ADCs in support of the final cost objective.

As another example, perhaps a project calls for the temporary relocation of a household while the removal of lead-based paint is performed for a housing rehabilitation project. Staff costs for those carrying out the relocation portion of activity could be considered part of the

ADCs for the housing rehabilitation activity as a whole. (See also the IDIS Matrix Code 14H definition regarding housing rehabilitation administration as activity delivery costs.)

CDBG funds may be used for ADCs in conjunction with other CPD formula grant activities (e.g., assisted with HOME, ESG, or HOPWA) where the activity is otherwise CDBG eligible and meets a national objective. But, because the activity is assisted in whole or in part with CDBG, it is subject to all CDBG rules and federal requirements in addition to those rules of the other grant programs. As stated above, however, this does provide for the use of CDBG funds for general PACs associated with the other formula programs.

## **2. Costs in support of the HOME Program**

Generally, new construction housing is an ineligible CDBG activity as set forth at 24 CFR 570.207. However, the use of CDBG in the support of HOME-assisted projects has been eligible since the enactment of CDBG statutory amendments made in 1992. Initially, the use of CDBG with HOME funds was subject to CDBG's 20 percent limit on general program administration. Subsequent statutory amendments removed this restriction. Section 105(a)(20) of the HCDA states that CDBG funds may be used to pay for housing services in support of HOME-assisted projects. This provision is codified in the CDBG regulations at 24 CFR 570.201(k).

Thus, while the use of CDBG for HOME program administration costs remained eligible under 24 CFR 570.206(g), it was clarified at 24 CFR 570.201(k) that the use of CDBG funds is an eligible use in support of a HOME-assisted project. The overall intent of this change was to provide for a broad array CDBG uses in support of HOME-assisted projects. The statute and 24 CFR 570.201(k) refers to CDBG eligible ADCs for HOME under the term "housing services." Housing services are eligible under 24 CFR 570.201(k). Eligible CDBG-HOME housing services include such things as housing counseling and tenant-based rental assistance, energy auditing, work specifications and architectural plans, loan processing, tenant selection, and other services related to assisting owners, tenants, third party entities participating or seeking to participate in a HOME project.

Please note, however, that the eligibility and benefit requirements of the CDBG and HOME programs differ in that the HOME term "project" and the CDBG term "activity" are not synonymous, and that care should be exercised in management and documentation when blending the two sources of funds on one activities.

## **3. Public Service Costs**

Staff costs for carrying out public services associated with another CPD program are also eligible providing that public service is eligible and meets a national objective. As an example, for a nonprofit organization providing health services to homeless persons or persons with AIDS, payment of the employee's salary delivering the services (rather than an Executive Director or Chief Operating Officer) would be eligible as part of carrying out the underlying public service. The provision of health services is a CDBG-eligible public service activity under Section 105(a)(8) and 24 CFR 570.201(e). Therefore the grantee may use CDBG funds to pay the

employee's salary that is carrying out the public service as an ADC, providing the non-profit meet the compliance requirements under the public service provision and the CDBG program in general. That is to say, if the activity is a new public service or a quantifiable increase in the level of an existing public service, staff costs allocable to CDBG are limited by the grantee's overall 15 percent public service cap.

[Note: Public service expenditures are limited to not more than 15 percent of a grantee's annual CDBG allocation plus 15 percent of their prior year's program income. This requirement is statutory under Section 105(a)(8) of the HCDA.]

#### **IV. DIRECT AND INDIRECT COSTS**

There is no universal rule for classifying certain costs as either direct or indirect under every accounting system. A cost may be direct with respect to a certain service or function, but indirect with respect to the Federal award or other final cost objective. Thus, certain indirect costs may be allocable as part of carrying out an eligible CDBG activity, such as housing rehabilitation, and appropriately identified and treated as ADCs. General guidelines for determining direct and indirect costs charged to Federal awards are provided at 2 CFR 225 (formerly OMB Circular A-87). A brief discussion of these costs categories follows.

*Direct costs* are those that can be identified specifically with a particular final cost objective. Typical direct costs chargeable to Federal awards are:

- a. Compensation of employees for the time devoted and identified specifically to the performance of those awards;
- b. Cost of materials acquired, consumed, or expended specifically for the purpose of those awards;
- c. Equipment and other approved capital expenditures;
- d. Travel expenses incurred specifically to carry out the award;

Any direct cost of a minor amount may be treated as an indirect cost for reasons of practicality where such accounting treatment for that item of cost is consistently applied to all cost objectives.

*Indirect costs* are those incurred for a common or joint purpose and benefiting more than one cost objective. They are not readily assignable to the cost objective specifically benefitting from the award without effort disproportionate to the results achieved. The term "indirect costs," as used by OMB, applies to costs that originate in the grantee's CDBG department and other departments that supply goods, services, and facilities for carrying out the CDBG program. Indirect costs examples are as follows:

- a. Central services costs, such as motor pools, computer centers, accounting office space leases, telephone service, utility bills, copy machines, etc.;
- b. Internal service costs, such as personnel, general administration, and purchasing;
- c. Legal costs and self-insurance costs; and
- d. Fringe benefit costs, such as pensions and health insurance.

In addition to restrictions contained in 2 CFR Part 225, there may be state or local laws that further limit the amount of administrative or indirect cost allowed. Moreover, amounts not recoverable as indirect costs or administrative costs allocable to one Federal award may not be shifted to another Federal award, unless specifically authorized by Federal legislation or regulation.

## **V. OTHER FINANCIAL MANAGEMENT REQUIREMENTS**

### **1. General**

The Office of Management and Budget (OMB) establishes cost principles to establish a uniform approach for determining costs to ensure effective and efficient program delivery. The most applicable sections to the CDBG program are the following: OMB Circular A-87 [relocated to 2 CFR Part 225], which contains the Cost Principles for State, Local and Indian Tribe Governments; and OMB Circular A-122 [relocated to 2 CFR Part 230], which contains the Cost Principles for Nonprofit Organizations. These cost principles are incorporated into the CDBG regulations by reference, but most substantially at 24 CFR 570.500 – 505.

The OMB basic guidelines apply to all federal agencies and address the following cost categories: allocable and allowable, reasonable costs, cost composition as a direct or indirect cost, and the treatment of applicable credits or offsetting costs. Accordingly, these principles effect the allocation of allowable staff costs to general administration activities or otherwise CDBG-eligible activity costs that are associated with a final cost objective. Generally, OMB advises that costs be accorded consistent treatment in order to enhance the likelihood that comparable costs are treated similarly in the application of cost accounting practices. OMB also advises that a cost may *not* be assigned to a Federal award as a direct cost if any other cost incurred for the same purpose in like circumstances has been allocated to the Federal award as an indirect cost. Attachment D provides paraphrased excerpts from OMB's Cost Principles.

### **2. Applicable Credits**

In general, applicable credits reduce the net amount of CDBG funds necessary to carry out an eligible CDBG activity (see 2 CFR part 225, Appendices A). Applicable credits refer to receipts or reductions of expenditure-type transactions that offset or reduce a cost item that is allocable to a Federal award as either a direct or indirect cost. To the extent that such offsets or credits are received by the governmental unit, they shall be credited to the Federal award either as a cost reduction or cash refund, as appropriate. Examples of transactions that generate applicable credits are the following:

- The collection of loan application fees associated with provisions of financial assistance to rehabilitate privately-owned multifamily housing [24 CFR 570.202]. Such fees are often collected to assure the applicant's commitment to providing the necessary underwriting and compliance documentation for the project;

- The collection of loan application fees for provisions of financial assistance to for-profit businesses [economic development activities at 24 CFR 570.203(b)]. Such fees are collected to assure a commitment from the applicant/borrower to provide documentation necessary for the grantee to conduct a prudent financial underwriting; and,
- Taking advantage of purchase discounts, rebates, or allowances, and accounting for adjustments for overpayments or erroneous charges associated with an eligible activity.
- Code enforcement fines, but only if (1) the cost of the code inspections and enforcement and/or the inspectors' salaries must have been wholly or partially paid for with CDBG funds, and (2) the intended purpose of the code enforcement fine (as reflected in local law, handbook, manual, etc.) is to recover the costs incurred for the code enforcement activities without regard to the source of funds for payment of the code enforcement activity.

## VI. CONCLUSION

Table 3 presents a snapshot of the relationships among costs. Appendix A provides instructions on how to calculate the amount that may be used for PACs for Entitlements. Appendix B provides a Functional Staff Cost Model. Appendix C provides the OMB Cost Definitions and Guidelines. Additional guidance may also be found in [The CDBG Guide to National Objectives and Eligible Activities](#), located on the web at: [http://portal.hud.gov/hudportal/documents/huddoc?id=DOC\\_17133.pdf](http://portal.hud.gov/hudportal/documents/huddoc?id=DOC_17133.pdf). Questions regarding this Notice should be directed to your local HUD Field Office.

Table 3 – Relationships Among Costs



## APPENDIX A

### Program Administration Cap Calculation for Entitlements

#### ***Description***

Not more than 20 percent of the sum of any grant plus program income that is received during the program year may be obligated by the grantee and its subrecipients for program administration costs, as defined in §570.205 and §570.206, respectively. Recipients of entitlement grants will be considered to be in conformance with this limitation if total obligations charged under those categories during the grantee's most recently completed program year, without regard to the source year of funds, are not greater than 20% of the sum of the entitlement grant received for that program year plus the program income received during that program year by the grantee and its subrecipients. [References: Appropriation Acts and §570.200(g)]

#### ***Calculating the Cap***

To determine the base against which the 20% cap will be applied, total the amount of CDBG funds *received during the program year* from the following sources:

#### ***Step 1***

(1) Entitlement Grant (from line 8.b of the Funding Approval form, HUD-7082):	\$ _____
(2) Surplus from Urban Renewal (from line 10.b of the Funding Approval form):	\$ _____
(3) Program income received by the grantee and its Subrecipients:	\$ _____
<b>(4) TOTAL</b>	<b>\$ _____</b>

#### ***Step 2***

(1) To calculate the <b>cap</b> amount, <i>multiply</i> the total amount determined in line (4) above by 0.20 and enter the number here:	\$ _____
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This amount represents **the cap**; it is the maximum dollar amount that may be obligated during the program year and charged to the eligible categories of program administration, §570.205 and §570.206, respectively.

## ***Determining Compliance with the Cap***

### ***Step 3***

Compliance with the cap is determined for entitlement grantees by performing the calculation below at the end of each program year, as follows:

- (1) Determine the total amount of CDBG funds expended during the program year for activities that are classified as eligible under §570.205 (Planning and Capacity Building) and §570.206 (Program Administration Costs): \$ \_\_\_\_\_
- (2) Add to the above amount the total amount of unliquidated obligations for activities under these same two categories, *as of the end of the program year*: \$ \_\_\_\_\_
- (3) Subtract from the balance the total amount of unliquidated obligations for these two categories, as of the *end of the preceding program year*: \$(\_\_\_\_\_ )
- (4) Enter here the result of the above calculations. This is the amount of net obligations for Program Administration during the program year: \$ \_\_\_\_\_

To be in compliance with the 20% cap, the amount determined above, as the net amount obligated, may not exceed the amount determined as the cap in Line for the year in the first portion of this subsection (see *Step 2* above).

Net amount obligated Line (4) above: \$ \_\_\_\_\_  
 Cannot be greater than the cap: \$ \_\_\_\_\_

## APPENDIX B

### Functional Staff-Cost Model

<b>HOUSING REHABILITATION PROGRAM</b>		<b>ALLOCABLE STAFF COSTS</b>	
<b>Staff Organization</b>	<b>Staff Function</b>	<b>Program Administration Costs</b>	<b>Activity Delivery Costs</b>
		<b>(24 CFR 570.205-206 and 570.489(a))</b>	<b>(24 CFR 570.201-204)</b>
<b>Grantee's CDBG Program Management</b>	To administer, plan, and carry out a CDBG-assisted community development program and related activities	General management of personnel tasked with oversight and coordination, monitoring and evaluation, reporting and audit compliance	When time is spent on the implementation of a specific CDBG-eligible activity
<b>Division/Program Director</b>	To oversee Support Staff and Line Staff in carrying out CDBG-funded eligible activities or program(s) as identified in the grantee's consolidated plan	General administration and program management of financial requirements, program- and activity-related staff, and overall activity implementation and outcome evaluation	Time spent carrying out specific CDBG-eligible activity work, such as conducting the environmental review, administering Davis-Bacon requirements, or overseeing relocation benefits
<b>Unit of General Local Government (UGLG) or Subrecipient Staff</b>	To carry out CDBG-funded projects and activities located in their jurisdiction as an urban county participant, or under a subrecipient agreement	General UGLG administration, financial requirements, reports, documentation and compliance records, monitoring and oversight	All project-related implementation activities per a written agreement between the grantee and UGLG, or subrecipient
<b>Project Managers</b>	To oversee Line Staff and Support Staff in the implementation and carrying out of eligible CDBG-funded projects and activities	General administration duties for program management, program planning and analysis, reporting, monitoring and evaluation	Oversee day-to-day specific CDBG-eligible activities: Underwriting loans, reviewing construction progress, processing contractor invoices, approving change orders
<b>Support Staff</b>	To carry out general capacities for program management, oversight, and coordination of the grantee's CDBG program	General administrative and planning, analysis, reports, program monitoring and evaluation, and audit compliance	Preparing contracts, loan documentation, processing contractor payments, loan repayments, recording liens and notices of completion
<b>Line Staff</b>	To carry out the implementation of CDBG-funded projects and activities	Planning and analysis, reports, program monitoring and evaluation, and audit compliance	Perform specific CDBG-eligible activity implementation work: loan processing, construction progress inspections, contractor payments, change order initiation
<b>Contractor</b>	To perform for compensation with regard to implementing and completing a CDBG-funded project on behalf of the grantee, UGLG, or subrecipient	N/A	Perform in accordance with a written contract between the grantee, unit of local government, subrecipient, or homeowner
<b>Homeowner</b>	To receive the benefits of a CDBG-assisted activity	N/A	N/A

## APPENDIX C

### OMB COST DEFINITIONS AND GUIDELINES

The terms and definitions provided below are derived from the Office of Management and Budget (OMB), which establishes principles and standards to provide a uniform approach for determining allocable and allowable costs to promote effective program delivery and efficiency. Heretofore, OMB guidance was set forth in Circular A-87, “Cost Principles for State, Local, and Indian Tribal Governments.” However, A-87 has recently been relocated to the federal regulations at 2 CFR Part 225. This was part of an initiative to provide the public with a central location for Federal government policies on grants and other financial assistance and non-procurement agreements (See website link below.) These definitions have been paraphrased to reflect relevant terms used for identifying and treating allowable costs applicable to the CDBG program. For the precise language that applies to any aspect, please go the following OMB website:

[http://www.whitehouse.gov/sites/default/files/omb/assets/omb/fedreg/2005/083105\\_a87.pdf](http://www.whitehouse.gov/sites/default/files/omb/assets/omb/fedreg/2005/083105_a87.pdf)

#### **DEFINITIONS**

1. *Cost* means an amount as determined on a cash, accrual, or other basis acceptable to the Federal awarding or cognizant agency. It does not include transfers to a general or similar fund.
2. *Cost objective* means a function, organizational subdivision, contract, grant, or other activity for which cost data are needed and for which costs are incurred.
3. *Final cost objective* means a cost objective, that has allocated to it both direct and indirect costs and is a final accumulation point. For example, this could be an eligible CDBG activity of rehabilitating a single-family dwelling that upon completion will meet a low- and moderate-income household national objective.
4. *Allocate* means to assign an item of cost or a group of items of cost, to one or more cost objectives, such as an eligible CDBG activity. This term includes both direct assignment of cost and the reassignment of a share of costs from an indirect cost pool, such as accounting services applicable to overall program PACS.
5. *Allocable costs.*
  - a. A cost is allocable to a particular cost objective if the goods or services involved are chargeable or assignable to such cost objective in accordance with relative benefits received.
  - b. All activities which benefit from the governmental unit’s indirect cost, including unallowable activities, will receive an appropriate allocation of indirect costs.
  - c. Any cost allocable to a particular Federal award or cost objective under the principles provided for in 2 CFR Part 225 may not be charged to other Federal awards to overcome fund deficiencies, to avoid restrictions imposed by law or terms of the Federal awards, or for other reasons.
  - d. Where an accumulation of indirect costs will ultimately result in charges to a Federal award, a cost allocation plan will be required as described in Appendices C, D, and E to this part.
6. *Allowable costs.* To be allowable under Federal awards, costs must meet several general criteria among them which are the following:
  - a. Be necessary and reasonable for proper and efficient performance and administration of the Federal award.
  - b. Be consistent with policies, regulations, and procedures that apply uniformly to both Federal awards and other activities of the governmental unit.
  - c. Be accorded consistent treatment. A cost may not be assigned to a Federal award as a direct cost if any other cost incurred for the same purpose in like circumstances has been allocated to the Federal award as an indirect cost.
  - d. Be adequately documented.

7. *Reasonable costs.* A cost is reasonable if, in its nature and amount, it does not exceed that which would be incurred by a prudent person under the circumstances prevailing at the time the decision was made to incur the cost. In determining reasonableness of a given cost, consideration shall be given to whether the cost is of a type generally recognized as ordinary and necessary for the operation of the governmental unit or the performance of the Federal award.
  - a. Whether the cost is of a type generally recognized as ordinary and necessary for the operation of the governmental unit or the performance of the Federal award.
  - b. The restraints or requirements imposed by such factors as: Sound business practices; arm's-length bargaining; Federal, State and other laws and regulations; and, terms and conditions of the Federal award. All activities which benefit from the governmental unit's indirect cost, including unallowable activities, will receive an appropriate allocation of indirect costs.
8. *Applicable credits.* Applicable credits refer to those receipts or reduction of expenditure-type transactions that offset or reduce expense items allocable to Federal awards as direct or indirect costs. Examples of such transactions are: Purchase discounts, rebates or allowances, recoveries or indemnities on losses, insurance refunds or rebates, and adjustments of overpayments or erroneous charges. To the extent that such credits accruing to or received by the governmental unit relate to allowable costs, they shall be credited to the Federal award either as a cost reduction or a cash refund, as appropriate.

#### ***Cost Composition***

9. *Total cost.* The total cost of Federal awards is comprised of the allowable direct cost to the CDBG program, plus its allocable portion of allowable indirect costs, less applicable credits.
10. *Classification of costs.* There is no universal rule for classifying certain costs as either *direct or indirect* under every accounting system. A cost may be direct with respect to some specific service or function, but indirect with respect to the Federal award or other final cost objective. Therefore, it is essential that each item of cost be treated consistently in like circumstances either as a direct or an indirect cost. Guidelines for determining direct and indirect costs charged to Federal awards are provided in the section 2 CFR 225.

#### ***Direct Costs***

11. *Direct costs* are generally those that can be identified specifically with a particular final cost objective. Examples of direct costs chargeable to Federal awards are:
  - a. Compensation of employees for the time devoted and identified specifically to the performance of those awards.
  - b. Cost of materials acquired, consumed, or expended specifically for the purpose of those awards.
  - c. Equipment and other approved capital expenditures.
  - d. Travel expenses incurred specifically to carry out the award.
12. *Minor items.* Any direct cost of a minor amount may be treated as an indirect cost for reasons of practicality where such accounting treatment for that item of cost is consistently applied to all cost objectives.

#### ***Indirect Costs***

13. *Indirect costs* are those: Incurred for a common or joint purpose benefiting more than one cost objective, and not readily assignable to the cost objectives specifically benefitted, without effort disproportionate to the results achieved. The term "indirect costs," applies to costs of this type originating in the grantee department, as well as those incurred by other departments in supplying goods, services, and facilities. To facilitate equitable distribution of indirect expenses to the cost objectives served, it may be necessary to establish a number of pools of indirect costs within a governmental unit department or in other agencies providing services to a governmental unit department. Indirect cost pools should be distributed to benefitted cost objectives on bases that will produce an equitable result in consideration of relative benefits derived.
14. *Cost allocation plans and indirect cost proposals.* Requirements for development and submission of cost allocation plans and indirect cost rate proposals are contained in Appendices C, D, and E to 2 CFR Part 225.
15. *Limitation on indirect or administrative costs.*

- a. In addition to restrictions contained in 2 CFR Part 225, there may be laws that further limit the amount of administrative or indirect cost allowed.
- b. Amounts not recoverable as indirect costs or administrative costs under one Federal award may not be shifted to another Federal award, unless specifically authorized by Federal legislation or regulation.

16. *Interagency Services*. The cost of services provided by one agency to another.