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OFFICE OF MANAGEMENT AND BUDGET

2 CFR Chapters I and II

Reform of Federal Policies Relating to Grants and Cooperative Agreements; Cost Principles and Administrative Requirements (Including Single Audit Act)

AGENCY: Executive Office of the President, Office of Management and Budget (OMB).

ACTION: Proposed Guidance.

SUMMARY: To deliver on President Obama's promise of a 21st-Century government that is more efficient, transparent, and creative, the Office of Management and Budget (OMB) is seeking to adjust the Federal government's partnership with non-Federal stakeholders to best achieve program outcomes while we ensure the financial integrity of the dollars we spend. The goal of this effort is to transform our Federal financial assistance framework so that it meets a higher standard of performance on behalf of the American people.

OMB proposes these reforms to the guidance for Federal policies relating to grants in order to ensure that Federal grants meet the high standards of a 21st-Century government. Federal grant-making must be streamlined to make the most of taxpayer dollars and ensure financial integrity while delivering the right program outcomes. This proposal provides this opportunity for the Federal government and its partners: state, local, tribal governments, institutions of higher education, and nonprofit organizations, to rethink and reform the rules that govern our stewardship of Federal dollars.

DATES: To be assured of consideration, comments must be received by OMB electronically through www.regulations.gov no later than midnight Eastern Standard Time (E.S.T) on [Insert date 90 days after date of publication in the Federal Register].

ADDRESSES: Comments on this proposal must be submitted electronically at www.regulations.gov. In submitting comments, please search for recent submissions by OMB to find docket OMB-2013-0001, which includes the full text of this proposal, and submit comments there.

Comments will be most useful if they are presented in the same sequence and with the same section number as the section of this guidance to which they apply. Please also provide any information regarding the cost implications of any particular proposal. If you are submitting comments on behalf of an organization, please identify the organization, and if that organization represents a number of entities, please note the number of entities who endorse the organization's comments. Finally, the public comments received by OMB will be posted at <http://www.regulations.gov> (follow the search instructions on that website to view public comments). Accordingly, please do not include in your comments any confidential business information or information of a personal-privacy nature.

To View This Proposal: The complete text of this proposal and a crosswalk of policy changes from the existing guidance are available on the OMB website at http://www.whitehouse.gov/omb/grants_docs under "Proposed Policies" and will also be available on www.regulations.gov by searching for docket number OMB-2013-0001, or, in hard copy, by contacting Victoria Collin of OMB at (202) 395-7791. Copies of the OMB Circulars that are discussed in

this notice are available on OMB's website at http://www.whitehouse.gov/omb/circulars_default/.

FOR FURTHER INFORMATION CONTACT: For general information, please contact Victoria Collin at (202) 395-7791. OMB will host an informational webcast with the Council on Financial Assistance Reform and key stakeholders on Friday February 8th, 2013 at 11:00AM EST available at www.cfoc.gov. More information on the Council on Financial Assistance Reform is available at www.cfo.gov/cofar.

SUPPLEMENTARY INFORMATION:

With this proposal, OMB seeks to ensure the highest integrity in the financial management and operation of federal programs and to strengthen accountability for Federal dollars by improving policies that protect against waste, fraud, and abuse. At the same time, OMB aims to increase the impact and accessibility of programs by minimizing time spent complying with unnecessarily burdensome administrative requirements, and so to re-orient recipients toward achieving program objectives. Through close and sustained collaboration with Federal and non-Federal partners, OMB has developed ideas articulated in

this proposal that would ensure that grants are awarded based on merit; that management increases focus on performance outcomes; and that rules governing the allocation of Federal fund are streamlined, and better focus the Single Audit oversight tool to reduce waste, fraud, and abuse.

This proposal—the complete text of which is available online, or in hard copy by telephone request (see *To View This Proposal* section)—follows the February 28, 2012 Advance Notice of Proposed Guidance (ANPG) published in the Federal Register. Both that notice and this proposal were developed in response to the November 23, 2009 Executive Order 13520 on *Reducing Improper Payments* and his February 28, 2011 Presidential Memorandum on *Administrative Flexibility, Lower Costs, and Better Results for State, Local, and Tribal Governments*. In those documents, the President directed OMB to work with Executive Branch agencies; state, local, and tribal governments; and other key stakeholders to evaluate potential reforms to Federal grants policies. The ANPG built on the work of those collaborations and discussed initial ideas to meet those goals. OMB received over 350 responses to the notice from across the spectrum of stakeholders in the grants

community. The notice and comments received in response are available to the public at www.Regulations.gov under docket number OMB-2012-0002.

This proposal was developed after considering the comments received in response to the ANPG. This preamble outlines the broad themes of stakeholder feedback received and how that feedback influenced further development of ideas mentioned in the ANPG into this proposal. With this publication, the public is once again invited to comment on the proposed reforms. Comments received in response to this proposal will be used to further refine the reforms discussed prior to the issuance of new guidance.

This proposed guidance would supersede and streamline requirements from OMB Circulars A-21, A-87, A-110, and A-122 (which have been placed in 2 CFR Parts 220, 225, 215, and 230); Circulars A-89, A-102, and A-133; the guidance in Circular A-50 on Single Audit Act follow-up; and pending further review, the Cost Principles for Hospitals at 45 CFR Part 74, Appendix E. The proposal consolidates the guidance previously contained in the aforementioned citations into a streamlined and consolidated format that aims to improve both the clarity and accessibility of the

guidance. If and when this proposal is finalized, OMB will integrate this guidance into Title 2 of the Code of Federal Regulations.

Similar to existing guidance that this proposal would supersede, the new guidance would be applicable to grants and cooperative agreements that involve state, local, and tribal governments as well as institutions of higher education, and nonprofit organizations. Parts of it may also apply to for-profit entities in limited circumstances as described in section .101 Applicability and the Federal Acquisition Regulation. Single Audit Act requirements will continue to apply to all Federal awards, including contracts, though cost-reimbursement contracts may continue to be subject to additional audit requirements. This guidance does not supersede any existing authority under law or by executive order or the Federal Acquisition Regulation.

I. Objectives and Background

A. Objectives

OMB is proposing new streamlined guidance for grants in order to meet the standards of a high-performing 21st-Century government. Only by streamlining this guidance can we increase the efficiency and effectiveness of the Federal grant-making process to ensure best use of the more than \$500 billion in Federal funds that are spent through grants.

As the President articulated in Executive Order 13563 of January 18, 2011, on *Improving Regulation and Regulatory Review* (76 FR 3821; January 21, 2011; <http://www.gpo.gov/fdsys/pkg/FR-2011-01-21/pdf/2011-1385.pdf>), each Federal agency must "tailor its regulations to impose the least burden on society, consistent with regulatory objectives, taking into account, among other things, and to the extent practicable, the costs of cumulative regulations." To that end, it is important that Federal agencies identify those "rules that may be outmoded, ineffective, insufficient, or excessively burdensome," and "modify, streamline, expand, or repeal them in accordance with what has been learned." The President reinforced his commitment in Executive Order 13579 of July 11, 2011 on *Regulation and Independent Regulatory Agencies* (76 FR 41587; July 14, 2011;

<http://www.gpo.gov/fdsys/pkg/FR-2011-07-14/pdf/2011-17953.pdf>).

As in other areas involving Federal requirements, the President is committed to making government more accountable to the American people while eliminating requirements that are unnecessary and reforming those requirements that are overly burdensome. Eliminating unnecessary requirements for financial assistance will allow recipients of Federal awards to re-orient efforts spent on compliance with complex requirements towards achievement of programmatic objectives. As part of this commitment, the President believes that the Federal government has an obligation to eliminate roadblocks to effective performance in carrying out and completing grants and cooperative agreements. Essential to this reform effort is reducing "red tape" that is attached to the financial assistance the Federal government provides annually in the form of grants and cooperative agreements. These awards provide important benefits and services to the public, and most of the awards go to state, local and tribal governments as well as to institutions of higher education, hospitals, and non-profit organizations. In order to ensure that the public receives the most value, it

is essential that these programs function as effectively and efficiently as possible, and that there is a high level of accountability to prevent waste, fraud, and abuse.

To this end, the President on February 28, 2011, issued his Memorandum on *Administrative Flexibility, Lower Costs, and Better Results for State, Local, and Tribal Governments*, (Daily Comp. Pres. Docs.;

<http://www.gpo.gov/fdsys/pkg/DCPD-201100123/pdf/DCPD-201100123.pdf>). In the Memorandum, the President

explained that "Federal program requirements over the past several decades have sometimes been onerous, and they have not always contributed to better outcomes. With input from our state, local, and tribal partners, we can, consistent with law, reduce unnecessary regulatory and administrative burdens and redirect resources to services that are essential to achieving better outcomes at lower cost." In addition to other actions, the President instructed the OMB Director to "review and where appropriate revise guidance concerning cost principles, burden minimizations, and audits for state, local, and tribal governments in order to eliminate, to the extent permitted by law, unnecessary, unduly burdensome, duplicative, or low-priority recordkeeping requirements and effectively tie such

requirements to achievement of outcomes." OMB has endeavored to deliver on that mission with this proposal.

Equally as essential to a 21st-Century government as removing unnecessary and overly burdensome requirements that interfere with efficient and effective program performance is strengthening accountability by "intensifying efforts to eliminate payment error, waste, fraud, and abuse" in Federal programs, as the President emphasized in Executive Order 13520 of November 20, 2009, on *Reducing Improper Payments* (74 FR 62201; November 25, 2009; <http://www.gpo.gov/fdsys/pkg/FR-2009-11-25/pdf/E9-28493.pdf>). Accordingly, as the President explained, it is important for Federal agencies "to more effectively tailor their methodologies for identifying and measuring improper payments to those programs, or components of programs, where improper payments are most likely to occur." This proposed guidance is aimed at achieving these goals by focusing our Single Audit tool on the programs and practices that pose the greatest risk of improper payments, waste, fraud, and abuse.

This proposal would streamline the language from eight existing OMB circulars into one document. This

consolidation is aimed at eliminating duplicative or almost duplicative language in order to clarify where policy is substantively different across types of entities, and where it is not. As a result, the proposed guidance includes sections and parts of sections which are clearly delineated by the type of entity to which they apply. For Federal agencies, auditors, and pass-through entities that engage with multiple types of entities in the course of managing grants, this consolidation is intended to clarify where policies are uniform across entities or differ, protecting variances in policy where required by the unique nature of each type of entity.

Accordingly, section .101 Applicability outlines how each subchapter of the proposed circular will apply across types of entities. All provisions of this circular would apply uniformly to grant and cooperative agreement awards made to state, local, and tribal governments, institutions of higher education, and nonprofit organizations except where specific variations by entity are described within this circular. The provisions of Subchapter G Audit Requirements will apply to all awards made to the above-mentioned types of entities as described in section .702 Basis for Determining Federal Award Expenditures. These

provisions would apply equally to recipients and subrecipients receiving Federal awards. The proposal states that Federal agencies may apply the provisions of Subchapters B through F to commercial organizations, foreign governments, organizations under the jurisdiction of foreign governments, and international organizations. The provisions of subchapter G would not apply to non-U.S.-based entities expending Federal awards. OMB may consider providing further guidance in the future around best practices for applying the policies in subchapters B-F to commercial and non-U.S. based entities.

OMB is interested in receiving broad public feedback to further refine these ideas. Comments received will be considered as OMB develops a refined final guidance document. Following the implementation of these reforms, OMB will continue to monitor their effects to evaluate whether (and the extent to which) the reforms are achieving their desired results, and will consider making further modifications as appropriate.

B. Background

This proposal reflects input from over a year of work by the Federal and non-Federal financial assistance community. In response to the President's direction that OMB and Federal agencies identify ways to make the oversight of Federal funds more effective and more efficient, OMB worked with the Office of Science and Technology Policy (OSTP) to convene meetings with both Federal and non-Federal stakeholders to discuss possible reform efforts. These meetings resulted in OMB receiving a series of reform ideas in late 2011 that were developed into the ANPG published on February 28th, 2012. That notice and the more than 350 comments received in response to it are available to the public on www.regulations.gov.

On October 27, 2011, the OMB Director issued Memorandum M-12-01, *Creation of the Council on Financial Assistance Reform*

(<http://www.whitehouse.gov/sites/default/files/omb/memoranda/2012/m-12-01.pdf>). To "create a more streamlined and accountable structure to coordinate financial assistance," the Memorandum established the interagency Council on Financial Assistance Reform (COFAR) as a replacement for two Federal boards (the Grants Policy Council and the Grants Executive Board). The 10-member COFAR is composed

of OMB's Office of Federal Financial Management (Co-Chair); the eight largest grant-making agencies, which are the Departments of Health and Human Services (a Co-Chair), Agriculture, Education, Energy, Homeland Security, Housing and Urban Development, Labor, and Transportation; and one additional rotating member to represent the perspectives of other agencies, which for the first two-year term is the National Science Foundation.

As the COFAR begins to solidify its role in the grants community, it has committed to engaging in outreach efforts with both Federal and non-Federal stakeholders, both in response to this proposal and going forward. Since the COFAR's first meeting on November 4, 2011, and through its review of the comments received in response to the ANPG, it has worked to formulate and further develop reform ideas to create the 21st-Century version of financial management policy for Federal assistance awards. These reform ideas as presented originally in the February notice, the broad themes of comments that were received in response to them, and the refined proposals presented here are outlined below in Part II of this notice. Part III is the actual draft text of the proposed guidance.

II. Reform Ideas Discussed in the Advance Notice of Proposed Guidance

In the ANPG, OMB invited comments from the public on all issues addressed in the advance notice, and further invited the public to make suggest additional reform suggestions. The goal of publishing the ANPT was to provide the broadest possible collection of stakeholders in the grants community with visibility on these ideas and the opportunity to participate in the discussion.

In response to the notice, OMB received more than 350 comments which were carefully considered in the development of this proposal. Accordingly, this section will continue the discussion by outlining the ideas that were proposed in the advance notice, the broad themes identified in the comments that were received across stakeholders, and the resulting reforms that OMB is proposing in this guidance. In addition, this section addresses particularly popular ideas for reform beyond the ANPG that were proposed by commenters and considered by OMB.

OMB views this proposal as an important opportunity to solicit stakeholder feedback, and the first opportunity for

the public to comment on specific language under consideration. The language proposed here is subject to revision; the feedback received will influence the extent to which this language becomes final. In some cases, we have noted in this section where there is language in the proposal that was particularly difficult to craft, and where feedback on the policy direction outlined will be especially useful in charting the future path.

The reform ideas under discussion are outlined below in four main categories:

1. Section A: Reforms to Administrative Requirements (the government-wide Common Rule implementing Circular A-102; Circular A-110; and Circular A-89)
2. Section B: Reforms to Cost Principles (Circulars A-21, A-87, and A-122)
3. Section C: Reforms to Audit Requirements (Circulars A-133 and A-50)
4. Section D: Additional Suggestions Outside of the Guidance Reform

In addition, more minor changes are listed in the crosswalk provided on the OMB website with this proposal.

Section A: Reforms to Administrative Requirements (the Common Rule implementing Circular A-102); Circular A-110; and Circular A-89: Subchapters A-E.

This section discusses proposed changes to the government-wide common rule implementing Circular A-102 on *Grants and Cooperative Agreements with State and Local Governments*; Circular A-110 on *Uniform Administrative Requirements for Grants and Other Agreements with Institutions of Higher Education, Hospitals and Other Non-Profit Organizations* (2 CFR part 215); and Circular A-89 on *Catalog of Federal Domestic Assistance*. The following are ideas for reform that were discussed in the February 28th Advance Notice of Proposed Guidance.

1. Creating a consolidated, uniform set of administrative requirements: Subchapters A-E

The ANPG solicited comments on consolidating the administrative requirements in OMB Circulars A-102 and A-110 into a uniform set of administrative requirements for all grant recipients.

The goal of this consolidation would be to eliminate duplicative (or almost duplicative) language while

clarifying where there are important substantive policy variances across entities. This consolidation is aimed at eliminating confusion for entities- such as Federal agencies, auditors and pass-through entities- that deal with more than one type of grant-recipient entity, and for whom greater clarity about which language is universal and which is not could be useful. Further, this language has been updated to reflect common 21st-Century business practices, such as electronic submissions of information, and to anticipate an even greater reliance on advances in information technology to move, store, and share data in the future. Finally, consolidation of the guidance aims to ensure that references across the guidance to other topics and sections are streamlined to most efficiently facilitate the understanding of complete policies.

Comments received in response to this idea in the ANPG fell broadly into two categories. Those commenters who deal habitually with more than one type of grant-recipient entity were generally in favor or open to consolidation, noting that consolidating duplicative or similar language and clarifying policy differences would relieve administrative burden. Other entities were less likely to see any potential benefit from the consolidation.

Some responders expressed concern that consolidation of circulars could lead to the broader application of onerous policies that previously had applied to a narrow set of entities. OMB has endeavored to craft the proposed language in such a way as to avoid this outcome, but will appreciate feedback if there are places where policies have inadvertently been broadened in an unfavorable way. Other responders worried that consolidation of the circulars might make it more difficult to make future changes that may only be applicable to one set of entities. OMB is sensitive to this concern, and believes that we will be able to remain responsive to the needs of all stakeholders through the ongoing outreach efforts of the COFAR, regardless of the level of integration of guidance in the circulars.

In this proposal, Subchapters A-E consolidate the administrative requirements as discussed. In drafting the consolidated version of the administrative requirements, OMB for the most part used language from OMB Circular A-110, and then endeavored to explicitly articulate where there were separate provisions for state, local, and tribal governments carried over from A-102, as described in the crosswalk published on the OMB website with this notice. In

section .504 Procurement standards, sections .40-.41 of A-110 were replaced with section .36 of A-102. OMB will be particularly interested in feedback from entities previously subject to the provisions of A-110 as to whether the new provision would result in increased administrative burden.

2. Requiring pre-award consideration of each proposal's merit and each applicant's financial risk: section .205 Agency Review of Merit of Proposals and Risk Posed by Applicants

The ANPG solicited comments on requiring agency consideration of the merit of each proposal and the financial risk associated with each applicant prior to making an award. The goal of this requirement would be to articulate as a government-wide policy a set of policies that, though widely practiced, have not previously been universally required across Federal agencies. Requiring agencies to design and implement a merit-based review process and to transparently disclose the criteria for that review in notices of funding availability will help ensure that all applicants for Federal assistance are guaranteed a fair and consistent review, and that they have the information they need to craft the strongest possible

applications. Further requiring agencies to review the financial risk posed by applicants will ensure that agencies are able to take appropriate steps to provide oversight for the award to mitigate any risks that may be present. This could supplement the oversight provided by audit activities which take corrective action well after the funds have been spent, and could result in complementary pro-active prevention of waste, fraud, and abuse.

Some of the comments received indicated concern that the proposal could hamper effective review policies and practices that agencies currently use. OMB has endeavored in crafting this language to ensure that these requirements do nothing to constrict the policies of agencies that already have robust review processes in place. As drafted, the requirements for merit-based review and financial risk review are separate and distinct, and each provides great flexibility to agencies.

Tribal entities expressed concern that this policy could contravene the requirements of the Indian Self-Determination and Education Assistance Act (ISDEAA). OMB notes that where the requirements in this guidance (and any OMB guidance) conflict with Federal statute, the statute

always governs. These proposals should be read as applicable only when they do not conflict with existing statutes, as described in section .101 Applicability.

Many commenters noted that the requirements of the Single Audit Act should already provide agencies with all necessary information about financial risk. Indeed, the proposed guidance includes Single Audit reports as one type of information that agencies may use in these reviews, but further options are available in the event that, for a particular set of circumstances, the Single Audit is not the most appropriate tool.

In this proposal, section .205 Agency Review of Merit of Proposals and Risk Posed by Applicants includes this requirement as discussed. The language in the proposal intentionally provides significant flexibility to agencies with respect to how these requirements are implemented. In particular, the requirement for an assessment of risk may be conducted at any point prior to an agency making an award, and therefore need only include review of applications likely to be selected for funding. OMB believes that this flexibility is important given the diverse nature of Federal programs and the types of information that might be most appropriate in different

cases. Recognizing that these reviews can be equally burdensome for both Federal agencies and for recipients, OMB expects that agencies will not to use this latitude to design overly burdensome requirements.

3. Requiring agencies to provide 90-day notice of funding opportunities: sections. 203 Requirement to Provide Public Notice of Federal Financial Assistance Programs and .204 Announcements of Funding Opportunities

The ANPG discussed requiring Federal agencies to provide 90-day advance forecast of funding opportunities in an updated Catalog of Federal Financial Assistance (CFFA) that would replace the existing Catalog of Federal Domestic Assistance (CFDA). The goal of this reform would be to provide applicants with enough time to prepare the best possible applications. At the time of the Federal Register Notice, OMB suggested that the CFFA, as an existing database of Federal programs, might be the most efficient tool to implement this requirement.

Many Federal agencies noted that implementation of a 90-day advance notice would be impossible in the event that appropriations take place late in the fiscal year, in which case agencies need to publish funding opportunities as soon as possible. Given the frequent need for agencies to

publish solicitations expeditiously after appropriations, OMB proposes to help ensure that applicants have adequate time to apply by instead articulating a minimum amount of time for the solicitation to be open on grants.gov.

Generally, comments received from recipient entities were in favor of providing applicants with as much time as possible to craft quality applications.

This proposal replaces the idea of 90-day advance notice in the CFFA with a requirement to ensure that all notices of funding opportunity be open for a minimum of 30 days on grants.gov, unless required by statute or unless exigent circumstances dictate otherwise as determined by the agency head. This language is proposed in section .204 Announcements of Funding Opportunities.

This proposal also refers to the Catalog of Federal Domestic Assistance by using the new name of the Catalog of Federal Financial Assistance. The final decision to change the name will be made in the context of ongoing COFAR governance of the Integrated Acquisition Environment and System for Award Management which currently hosts the CFDA and other governmentwide systems that support the grants community. This process will include consideration of any relevant system-related consequences to a name change.

In addition to these proposed changes to guidance, OMB is working with Federal agencies on the development of the Federal Program Inventory (FPI) over the course of 2013-2014. The FPI uses a broader definition of Federal Program than the definition proposed in this guidance, which refers specifically to the CFFA. The Federal Program Inventory will likely include linkages to CFFA. For more detail on the FPI see A-11 Part 6 Section 280.

4. Providing a standard format for announcements of funding opportunities: section .204 Announcements of Funding Opportunities

The ANPG discussed incorporating into circulars the existing requirement for certain categories of information to be published in announcements of public funding opportunities. See OMB Memorandum M-04-01 of October 15, 2003 (http://www.whitehouse.gov/omb/memoranda_fy04_m04-01), which announced the Federal Register notice that OMB published at 68 FR 58146 (October 8, 2003).

This is not a policy reform, but rather consolidation within the circular of separate guidance implemented in 2003 to further consolidate all applicable guidance for grants into one clear location.

Most comments received in response to the Advance Notice were generally in favor or had no objections to this consolidation.

This proposal incorporates this requirement in section .204 Announcements of Funding Opportunities.

5. Reiterating that information collections are subject to Paperwork Reduction Act approval: section .206 Standard Application Requirements

The ANPG discussed that information collection requests are limited to standardized data elements approved by OMB, as required under the Paperwork Reduction Act of 1995 (PRA), plus OMB-approved exceptions for all applications and reports. This is not a policy reform, but rather an indicator of the importance OMB places on compliance with the requirements of the Paperwork Reduction Act of 1995, and an indication that OMB will be using the PRA process to ensure that agencies make use of standard approved collections wherever possible to encourage broader goals of data standardization across government. As this standard of review is implemented, Federal agencies may find that fewer non-standard information collections are approved, if not required by statute.

Comments in response to the ANPG generally did not object to continued use of the Paperwork Reduction Act. Some comments emphasized in particular that use of government-wide systems to support information collections, such as Grants.gov, should be consistently funded and supported as standardization of information collections continues.

This proposal includes this language in section .206 Standard Application Requirements. In addition, the proposed language eliminates references to specific OMB-approved forms, and refers only broadly to OMB-approved information collections. This proposed language is not intended to have an immediate effect on the forms used, but is intended to broaden applicability so that, as the Federal government replaces forms with electronic collections of data elements, this guidance will continue to apply. Final guidance will be accompanied by a full list of the OMB-approved information collections that are available. For example, where section ____ .206 Standard Application Requirements refers to "the information approved by OMB for governmentwide use for applications," the list accompanying final guidance will refer section 206 to the 424 family of forms and any other OMB-approved information collections for applications, though in the

future, the data currently included in the 424 forms may be collected differently.

6. Additional Suggestions for Administrative Requirements:

In response to the ANPG, OMB received a number of suggestions for ways that existing guidance could be clarified. OMB reviewed these and anticipates that clarifications made in the draft language in subchapters A-E may address many of them. The most notable clarifications are as follows:

A. Subchapter C Federal Award Notice and Subchapter D Inclusion of Terms and Conditions in Federal Award Notice lay out mostly new uniform requirements for the information that agencies are required to provide to recipients at the time that an award is made. This language is based on work done by the Grants Executive Board and Grants Policy Committee, two interagency councils that preceded the COFAR in providing policy leadership to the grants community. In particular, this language includes the requirement to include a unique award identifier in the notice. OMB will continue working with Federal agencies to provide further guidance on the inclusion of this data element.

B. Section 501 Subrecipient Monitoring and Management is created to co-locate guidance on oversight of subawards that previously was located in different places in different OMB Circulars. This is an attempt to provide greater clarity into the expectations for subaward oversight across the Federal government.

C. Language in section 502 Standards for Financial and Program Management and other minor language throughout the guidance is updated to align the objectives for performance monitoring and measurement with those described for Federal agencies in OMB Circular A-11.

D. Language in section .504 Procurement Standards (d) updates the threshold for small purchase procedures to be consistent with the simplified acquisition threshold at 41 U.S.C. 403(11) (currently at \$150,000).

E. Language in Section .506 Records and Retention (c)(1) is simplified to clarify that the 3-year period for retention of documents starts on the day the award recipient submits its final expenditure report.

F. Section .808 on Closeout adds language that Federal agencies complete all closeout actions for Federal awards no later than 180 days after the final report is received.

OMB will consider whether further guidance on closeout is needed.

Finally, some state government entities asked that the threshold for requirements applicable to equipment be raised above \$5,000, but further discussions indicated that the level of that threshold varies significantly at the state level. In order to provide for consistent award management across entities, OMB considers \$5,000 to continue to be the most appropriate level for this degree of accountability.

B. Reforms to Cost Principles (Circulars A-21, A-87, and A-122, and the Cost Principles for Hospitals): Subchapter F Cost Principles and Appendices IV-IX.

This section discusses proposed changes to the OMB cost-principle circulars that have been placed at 2 CFR Parts 220, 225, and 215 (Circulars A-21, *Cost Principles for Educational Institutions*; Circular A-87, *Cost Principles for State, Local and Indian Tribal Governments*; and Circular A-122, *Cost Principles for Non-Profit Organizations*), and, pending possible future review, to the Cost Principles for Hospitals that are in the regulations of the Department of Health and Human Services at 45 CFR

Part 75, Appendix E (*Principles for Determining Costs Applicable to Research and Development Under Grants and Contracts with Hospitals*). The following ideas for reform were discussed in the ANPG.

1. Consolidating the cost principles into a single document, with limited variations by type of entity: Subchapter F and Appendices IV through IX

The ANPG solicited comments on consolidating the cost principles in OMB Circulars A-21, A-87, and A-122, and the Cost Principles for Hospitals that are in the regulations of the Department of Health and Human Services at 45 CFR Part 75, Appendix E, into a uniform set of cost principles for all grant recipients.

The goal of this consolidation would be to eliminate duplicative (or almost duplicative) language while clarifying where there are important substantive policy variances across entities. This is aimed at eliminating confusion for entities such as Federal agencies, auditors, and pass-through entities that deal with more than one type of grant recipient entity, and for whom greater clarity about which language is universal and which is not could be

useful. Further, the goal is to provide updated language to reflect common 21st-Century business practices, such as electronic submissions of information. Finally, consolidation of the guidance aims to ensure that references across the guidance to other topics and sections are streamlined to most efficiently facilitate the complete understanding of each policy.

Comments received in response to this idea in the ANPG fell broadly into the same two categories as those regarding consolidation of the circulars for administrative requirements. Those commenters who deal habitually with more than one type of grant recipient entity were generally in favor or open to consolidation, noting that consolidating duplicative or similar language and clarifying policy differences would relieve administrative burden. Other entities, in particular in the university community, who do not habitually deal with other types of grant recipients, were less likely to see any potential benefit from the consolidation.

Some responders expressed concern that consolidation of circulars into one set of guidance could lead to the broader application of onerous policies that previously had applied to a narrow set of entities. OMB has endeavored to

craft the proposed language in such a way as to avoid this outcome, but will appreciate feedback if there are places where policies have inadvertently been broadened in an unfavorable way. Other responders worried that the proposed consolidation might make it more difficult to make changes that would only be applicable to one set of entities. OMB is sensitive to this concern, and believes that we will be able to remain responsive to the needs of all stakeholders through the ongoing outreach efforts of the COFAR, regardless of the level of integration of guidance.

In this proposal, Subchapter F and Appendices IV-X consolidate the cost principles except those for hospitals, as discussed below. The majority of the consolidation is in Subchapter F, which outlines the basic considerations and the selected items of cost. Appendices IV-X provide specific guidance for negotiating indirect cost rates that varies by specific type of entity. Based on initial feedback, OMB proposes to conduct further review of the cost principles for hospitals, and will make a future determination about the extent to which they should be added in a reserved Appendix XI to this guidance based on the outcome of the review.

OMB will be particularly interested in feedback from the public on the language used in the consolidated cost principles, and whether any particular entity perceives a change in policy that appears unfavorable. OMB also notes that in response to concern from tribal entities that the consolidated cost principles may conflict with the cost principles provided in the ISDEAA, the subordination of this guidance to that statute was specifically articulated in section .101 Applicability.

2. For indirect ("facilities and administrative" or F&A) costs, using flat rates instead of negotiated rates:
section .616 Indirect (F&A) Costs

The ANPG discussed two different possibilities for offering flat indirect cost rates; one that would be a mandatory and universal discount from a negotiated rate, and a second that would give entities the option of choosing a flat discount from a previously negotiated rate.

The goal of this discussion was to explore whether the savings that could be accrued by avoiding the complexities of the negotiation process could be recaptured both by

recipients and Federal agencies through a slightly lower rate that would split the difference in the cost of the process evenly. It seemed that there could be a win-win amount that allowed the Federal government to pay a lower rate, but still provide an overall savings for recipients.

Commenters were universally against the idea of a mandatory flat discounted rate. Some who responded were in favor of having an optional flat rate, but almost all commenters indicated that if the flat rate were below the negotiated rate, it would almost always be worth it to negotiate for the difference.

Two new suggestions emerged that had not been discussed in the ANPG. One was to provide the option for entities and Federal agencies to agree to extend the period of utilization of a rate once negotiated. The second idea was proposed by the nonprofit community, and entailed explicitly requiring pass-through entities to honor rates that are negotiated at the Federal level.

Finally, some expressed interest in the availability of a minimum flat rate for entities that had never had a negotiated indirect cost rate. Such entities could adopt

this rate for an interim period, while developing capacity to engage in negotiations.

As a result of this feedback, this proposal does not further contemplate a flat negotiated rate, but rather provides in section .616 Indirect (F&A) costs for all types of entities the option of extending negotiated rates for up to 4 years subject to approval of the indirect cost cognizant agency. This one-time extension will only be approved if there have been no major changes in indirect costs. If an extension is granted the entity would not be allowed to request a rate review until the extension period ends. OMB hopes that this extension of the negotiated rate may provide a reduction in burden by reducing the frequency of negotiations.

In addition, also in section .616 Indirect (F&A) Costs, a minimum flat rate of 10% of modified total direct costs has been added to ensure that entities without the capacity for a full negotiation receive a minimum reimbursement for no more than four years while they develop the capacity to engage in full negotiations. Finally, section .501 Subrecipient Monitoring and Management explicitly requires pass-through entities to either honor the indirect cost

rates negotiated at the Federal level, negotiate a rate in accordance with Federal guidelines, or provide the minimum flat rate. This is aimed at ensuring that entities who receive Federal funds primarily indirectly nevertheless are appropriately reimbursed for the allowable costs associated with the award.

3. Exploring alternatives to time-and-effort reporting requirements for salaries and wages section .621 Selected Items of Cost, C-10 Compensation - Personal Services

The ANPG discusses OMB's intent to identify possible alternatives to current reporting requirements for validating the costs of salaries and wages. The discussion points to three pilots that are currently ongoing as possibly instructive examples of alternatives.

Consideration of alternatives to time and effort reporting reflects the long-term goal of tying assessment to the achievement of programmatic objectives rather than measurement of effort (hours) expended. OMB has learned that though this is an important long-term goal, based on the diverse nature of programs across the Federal government and related variations in methodologies for

measuring achievement and outcomes, time and effort reporting continues to be viewed by the audit community as an important tool for confirming appropriate use of funds.

In response to the ANPG, institutions of higher education in particular pointed out that current requirements are particularly restrictive because they include specific examples of compliance with current requirements which, over time, have become the rule. These commenters recommended broadening time and effort reporting language to omit specific examples and instead feature the essential principles for accountability based on strong internal controls that entities could then implement however is most appropriate for them. Some in the auditing community similarly commented that while open to streamlined guidance, they recommend OMB ensure that the standards for appropriate internal controls and audits remain clear.

This proposal addresses these ideas with language in section .621 Selected Items of Cost, item C-10 Compensation - Personal Services. Within this language, OMB has consolidated reporting requirements that previously differed across types of entities and eliminated specific examples in order to clarify the broad principles of how an entity may establish the internal controls that would allow

them to validate these costs. It recognizes the potential to integrate the necessary information in automated payroll distribution systems where clear internal controls govern those systems, thereby reducing duplication.

OMB will be interested in feedback from the audit community on whether the draft language provides sufficient guidance to result in a set of requirements that will be easily audited. Further, OMB will be interested in feedback from the recipient community on whether the language proposed adequately provides enough flexibility for entities to meet these standards in the way most appropriate to their particular organizations, and in ways that may change over time as technology continues to advance.

4. Revisions to reimbursements for utility costs to institutions of higher education. Appendix IV- Indirect (F&A) Costs Identification and Assignment, and Rate Determination for Educational Institutions

The ANPG discusses expanding the application of the 1.3% indirect (F&A) costs adjustment for utility costs of research to more institutions of higher education.

The goal of this reform idea would be to eliminate unfairness inherent in a policy that provides a benefit to a limited group of institutions based on arbitrary criteria without consideration of applicability to other institutions. The Utility Cost Adjustment (UCA) currently provides an extra 1.3% percentage points in addition to the negotiated indirect cost rate to 65 institutions of higher education for research grants. The ANPG noted that OMB would work with Department of Defense's Office of Naval Research and the Department of Health and Human Services' Division of Cost Allocation to develop guidelines and a format for entities to apply for this benefit in a streamlined way that ensured the adjustment was only provided where real costs exist. Further, the notice discussed requiring entities to demonstrate a plan to bring utility costs down over time.

The need for action is a result of the fact that utility costs, while included in indirect cost rate negotiations, are generally recorded only at the building level, making it difficult to document the utility cost that should be allocated to Federal awards as opposed to other activities. This is particularly true for research, where funded activities are likely to use more energy than teaching, for

example. The current situation is further complicated by the fact that the 1.3% adjustment itself is long outdated and based on limited information. Thus, there is a strong sense in the Federal community that some additional way to verify the accuracy of the adjustment is also overdue.

Commenters from the university community were in favor of expanding the adjustment, but many who currently receive the adjustment preferred that it not be expanded if the expansion would mean a reduction in funds to those who currently receive it, or in other words, a cost neutral expansion. Further, commenters argued strongly that the expansion should not be linked to a burdensome application or justification process, nor a burdensome process to document reductions in cost over time.

OMB has received feedback from rate setting agencies that given the complexities of documenting utility costs, it is likely that any type of study or application done to justify costs would be difficult to achieve with accuracy and without inducing significant administrative burden and expense for both recipient entities and Federal agencies.

As a potential solution, language in Appendix IV of this proposal would replace the 1.3% utility cost adjustment that is currently in effect with two options for reimbursement of utility costs. The first would allow any institution of higher education to meter their utility usage at the sub-building level instead of by building. When metering utility usage by function is not feasible, entities may add a multiplier to their square footage used for research to calculate "effective" square footage for purposes of utility cost calculation. Taken together, these two options should provide a more accurate reimbursement of utility costs through the normal indirect cost rate negotiation process than the current practice of metering by building does. OMB will be interested in responses to this proposal from institutions of higher education, particularly with regard to whether metering at the sub-building level within buildings is a feasible option for them or whether changes in metering practice are prohibitively expensive, the extent to which the calculation of the effective square footage is viewed as a fair proxy for utility costs, and whether this is likely to significantly increase the accuracy of utility cost reimbursements.

5. Charging directly allocable administrative support as a direct cost. Section .615 Direct Costs

The ANPG discussed clarifying the circumstances under which institutions of higher education and other entities where appropriate, may charge directly allocable administrative support as a direct cost. Included in this discussion were examples of appropriately direct chargeable project-specific activities such as managing substances such as chemicals, data and image management, complex project management, and security.

The goal of this reform idea was to ensure that charges are appropriately classified in order to provide support for all of the costs directly associated with a Federal award. It is further aimed at addressing a concern raised by institutions of higher education for which administrative tasks directly associated with a research grant routinely make up a significant proportion of directly-allocable activities and costs.

Comments received, including from the university community, indicated a preference that any further guidance rely on the overarching cost principles, which indicate that an item or activity may be charged directly to a grant if it is clearly allocable to that award, as opposed to an

activity that supports multiple projects. This principle remains true regardless of whether the work performed is administrative in nature.

This proposal reflects that principle, and guidance proposed in section .615 Direct Costs indicates that all work that is directly allocable to one award may be charged to that award, regardless of the type of task. With this proposal OMB hopes to provide consistently across the cost principles that direct costs are those allocable to one award, while indirect costs are those that cannot easily be so allocated.

6. Including the costs of certain computing devices as allowable direct cost supplies. Section .621 Selected items of cost, C-31 Material and Supplies Costs, Including Costs of Computing Devices

The ANPG discussed explicitly including the cost of computing devices not otherwise subject to inventory controls (i.e. cost less than the organization's equipment threshold) as allowable direct cost supplies. Applicants for Federal awards would be required to document these items as a separate line-item in their budget requests, but would not be required to conduct the more stringent inventory controls in place for equipment.

The goal of this clarification would be to ensure that charges are appropriately classified in order to provide support for all of the costs directly associated with a Federal award, while reducing the burdens of securing special permission to purchase what have become routine supplies. This is not intended to result in a net cost increase, but rather to provide clarity in how allowable costs are routinely charged. The need for this clarification is a result of the fact that while computing devices routinely cost less than the \$5,000 equipment threshold, they are seen as highly valuable items. These facts have led to diverse opinions as to whether these devices should be treated as equipment versus supplies, and to audit findings of incorrect documentation.

Commenters in the recipient community were generally in favor of this reform, but specified a preference that these items not require separate line items in budget requests as the ANPG contemplated. Those with this preference noted that specifying separate line items would limit existing rebudgeting authority in a way that would lead to less efficient administration of grants. The audit community argued in contrast that computing devices are both highly valuable and contain highly sensitive data, and so should

be subject to more detailed inventory requirements as they would be if classified as equipment. Others proposed that because these items may be used for more than one award, they should be treated as indirect costs.

This proposal discusses this idea in section .621 Selected items of cost, Item C- 31 Material and Supplies Costs, Including Costs of Computing Devices. The language proposed reflects feedback OMB received from Federal agencies that the sensitivity of data stored on computing devices should not be a factor in determining cost accounting, since protection of that data is a separate area of internal control. Recipient entities are responsible for the security and encryption of their data regardless of how the devices are accounted for. Further, the costs of documenting inventories for these items would be significant and generally detrimental to the efficient administration of the grant. Given the low cost of these items (generally far below the \$5,000 threshold) the proposed language anticipates that they fit naturally within the category contemplated as supplies, and should be explicitly included there, without further requirements to add a line item in the budget. Further, OMB believes these items are similar in their allocability to other items

typically in the supply category, which are directly allocable because of their programmatic relevance for the execution of an award, but which may have some unavoidable excess capacity.

7. Clarifying the threshold for an allowable maximum residual inventory of unused supplies. Section .621 Selected items of cost, C-31 Material and Supplies Costs, Including Costs of Computing Devices

The ANPG discussed harmonizing cost principles with existing language in Circulars A-110 and A-102 to clarify that \$5,000 is the threshold for an allowable maximum residual inventory of unused supplies as long as the cost was properly allocable to the original agreement at the time of purchase. The notice included language to the effect that these supplies may be retained for use on another Federal award at no cost, though that language did not align with existing guidance found in Circulars A-110 and A-102.

The goal of this clarification is to minimize confusion about appropriate disposal or re-expensing of unused inventories at the conclusion of an award and at ensuring consistency in the application of the cost principles.

Federal agencies view this requirement as important, because below this level the costs for the agency to recover, inventory, store, and dispose of these items would exceed the benefit of such efforts. Though the auditing community expressed some concern, particularly about what would be done when the recipient did not have another Federal award for which to retain the supplies, the majority of comments received on this idea were in favor of it.

This proposal clarifies language in section .621 Selected Items of Cost, Item C- 31 Material and Supply Costs, including Costs of Computing Devices. This language is harmonized with language in the draft administrative requirements that states that \$5,000 is the threshold for an allowable maximum residual inventory of unused supplies as long as the cost was properly allocable to the original agreement at the time of purchase. Consistent with existing administrative requirements, there is no requirement to retain the supplies for use on another Federal award.

8. Eliminating requirements to conduct studies of cost reasonableness for large research facilities. (No language in proposed guidance)

The ANPG discussed eliminating requirements for institutions of higher education, and other entities where appropriate, to conduct studies of cost reasonableness for large research facilities.

The goal of this reform would be to reduce paperwork that is costly to generate and duplicative of more useful information that is otherwise provided to the awarding agency. The cost reasonableness studies mentioned compare a specific set of data compared against a data set compiled by the National Science Foundation. This comparison does not yield information that is as useful as the information that is routinely reviewed by agencies any time a grant proposal includes a proposal for construction of a new facility. These routine reviews cover actual costs included in all aspects of the project, which program managers are able to evaluate using their expertise and knowledge of reasonableness of these proposals in comparison with others and with market prices. The specific studies in question have been found not to add additional value to this process.

Comments received in response to this idea were generally positive. This proposal eliminates the previously existing language.

9. Eliminating restrictions on use of indirect costs recovered for depreciation or use allowances. (No language in proposed guidance)

The ANPG discussed eliminating the restrictions on the use of the portion of indirect cost recoveries associated with depreciation or use allowances. These restrictions are duplicative of the indirect cost rate negotiation process, during which appropriate indirect costs are documented, justified, and negotiated. This requirement put restrictions on the use of funds which were received as reimbursements for costs already incurred appropriately in accordance with negotiated indirect cost rates.

Articulating requirements for how recipients should spend reimbursements is fundamentally duplicative.

Further, in this same item of cost, all references to use allowances have been eliminated. Use allowance was an alternative accounting method which was necessary at the time of the last update to OMB circulars because not all entities were capable of using the depreciation method. Now, however, the depreciation method is widely if not universally used, and use allowance has become an obsolete reference.

Comments received in response to this idea were generally positive. As a result, this proposal eliminates restrictions on depreciation reimbursements in section .621 Selected Items of Cost, item C-15 Depreciation.

10. Eliminating requirements to conduct a lease-purchase analysis for interest costs and to provide notice before relocating federally-sponsored activities from a debt-financed facility. (No language in proposed guidance)

The ANPG discussed eliminating requirements for institutions of higher education, and other entities where appropriate, to conduct a lease-purchase analysis to justify interest costs, and to notify the cognizant Federal agency prior to relocating federally sponsored activities from a facility financed by debt. The goal of this reform would be to reduce paperwork that is costly to generate and does not yield information that is useful to the awarding agency.

Where recipient entities are required to invest equity of their own in facilities they purchase, and where they must provide the up-front financing and are reimbursed based on the ongoing costs of facilities, OMB finds that entities have appropriate incentives to make the most cost-effective decisions about whether to lease or purchase a facility

without providing additional paperwork to the Federal government. Further, Federal agencies have provided feedback that such paperwork does not meaningfully affect funding decisions.

Comments received in response to this reform idea were generally positive. This proposal therefore eliminates this requirement.

11. Eliminate requirements that printed "help-wanted" advertising comply with particular specifications. Section .621 Selected Items of Cost, C-42 Recruiting Costs.

The ANPG discussed updating the cost principles to reflect the media now used for those notices. The goal of this reform would be to update guidance to conform to 21st-Century business processes. Comments received in response to this reform idea were generally positive.

This proposal updates this language accordingly, specifically in section .621 Selected Items of Cost, and item C-42 Recruiting Costs.

12. Allowing for the budgeting for contingency funds for certain awards. Section .621 Selected Items of Cost, C-12 Contingency Provisions.

The ANPG discussed clarifying that budgeting for contingency funds associated with a Federal award for the construction or upgrade of a large facility or instrument, or for IT systems, is an acceptable and necessary practice, and that the method by which contingency funds are managed and monitored is at the discretion of the Federal funding agency. The goal of this reform would be to ensure that contingencies inherent in grant-funded projects are planned for in accordance with Generally Accepted Accounting Principles (GAAP) and with standard project-management practices. The language seeks to accomplish this while making clear that reserve funds which recipients would draw down in advance of a particular event actually occurring, are unallowable.

Comments received in response to this reform idea were generally positive. Some in the audit community suggested limiting contingency budgets to a percentage of the total award; however, Federal agencies considered that this would be contrary to GAAP, and difficult to do at the government-wide level given the diverse nature of Federal programs. OMB acknowledges Federal agencies' program managers as experts in the particular needs of their programs, and expects them to look carefully at all award budgets,

including contingency budgets, to ensure that they are appropriate to the scope and scale of the project at hand. Some comments received indicated a preference for establishing advance draw-down reserve funds, but OMB finds that this would result in undue risk of improper payments, and additional administrative burden to recover such funds if they were not needed.

This proposal includes language to this effect in section. 621 Selected Items of Cost, C-12 Contingency Provisions.

13. Strengthening Requirements for all Recipients to Document Cost Accounting Practices and Provide Necessary Paperwork to Auditors While Eliminating Cost Accounting Standards and Requirement for Institutions of Higher Education to file a Disclosure Statement. Section .502 Standards for Financial and Program Management.

The ANPG discussed whether OMB should request that the CASB consider increasing from \$25 million to \$50 million in Federal awards per year (based on the average of an entity's three most recent years) the minimum threshold for institutions of higher education to file a cost accounting standards disclosure statement. Comments received in response to this reform idea were generally positive, though members of the university community argued that

institutions of higher education should not be subject to CAS requirements for financial assistance, since in the intent of these standards is duplicative of OMB guidance for grants but the language adds layers of complexity. Further, comments argued that universities should be exempt from requirements to file disclosure statements, on the basis that they are audited on the compliance of their internal policies with cost-accounting standards described in OMB guidance, making the added disclosure duplicative. Further, they find the process to obtain approvals of updates to the form itself to be often subject to frustrating delays. Comments from the auditing community indicate that any audit finding would ultimately rest on whether the entity's internal policies comply with OMB guidance, though some noted that the form itself provides a useful overview of cost accounting practices that have been pre-approved by the Federal government, providing a helpful starting point for any review. OMB recognizes that these requirements are applied solely to universities, posing an additional requirement on a particular group of entities without without a clear justification for singling out that particular group.

Ultimately, OMB finds it essential for all recipients to document their cost accounting standards and to provide auditors with any and all documentation required to satisfy audit inquiries. As a result, OMB has reviewed the proposed language in section .502 Standards for Financial and Program Management, paragraph (c). The existing requirement from A-110 that all recipients document their cost accounting practices remains sufficiently comprehensive and unchanged, but this proposal adds a cross reference to section . 506 on Record Retention and Access, which specifically authorizes awarding agencies, Inspectors General, and the Comptroller General of the United States to access these records. In addition, language has been added in section .708 Auditee Responsibilities to require recipients to provide auditors with any and all documentation required to complete the required audit. Finally, in the Single Audit Compliance Supplement, OMB would add language asking auditors to verify that recipients comply with the documentation requirements and to report any non-compliance appropriately as an audit finding.

OMB has also removed the CAS standards from the guidance, and eliminated the requirement for universities to file a

disclosure statement that must be approved by the awarding agency. This change applies only to the guidance for grants and cooperative agreements; this in no way alters requirements under the Federal Acquisition Regulation governed by the CASB that apply to entities receiving awards of contracts.

14. Allowing for excess or idle capacity for certain facilities, in anticipation of usage increases. Section .621 Selected Items of Cost, C-24 Idle Facilities and Idle Capacity

The ANPG discussed allowing for excess or idle capacity in consolidated data centers, telecommunications, and public safety facilities. The goal of this reform is to acknowledge the unique requirements inherent in consolidation of data centers as encouraged by the President in order to deliver a 21st-Century government. Data centers and other types of facilities require excess capacity at their creation in order to accommodate increases and fluctuations in usage later on. Other telecommunications facilities and public-safety emergency-response facilities have similar characteristics.

Comments received in response to this idea were generally positive. This proposal incorporates this idea in section

.621 Selected Items of Cost, item C-24 Idle Facilities and Idle Capacity.

15. Allowing costs for efforts to collect improper payment recoveries. Section .621 Selected Items of Cost, C-8 Collections of Improper Payments.

The ANPG discussed adding a new item of cost specifically to allow recipients to be reimbursed for expenses associated with the effort to collect improper payment recoveries or related activities. The goal of this reform is to better encourage recipient entities to assist the Federal government to meet the President's directive to improve the Federal government's ability to recover improper payments. The draft language is intended to allow recipients to keep an amount of funds collected to cover expenses of collection efforts, where the amount collected is likely to exceed the expense of collection.

These costs may be considered either indirect or direct costs as most appropriate for the entity in question. Amounts collected that exceed the expense of collection shall be treated in accordance with accepted cash management standards.

Though most comments received in response to this reform idea were generally in favor of it, some in the university community noted that where these are indirect costs, which are capped, additional allowability would not affect them. This proposal includes language in section .621 Selected items of cost, item C-8 Collections of Improper Payments to clarify allowable treatment of these costs.

16. Specifying that gains and/or losses due to speculative financing arrangements are unallowable. (No language in proposed guidance)

The ANPG discussed adding an item of cost to the guidance to clarify that gains or losses related to debt arrangements on capital assets due to speculative financing arrangements (such as hedges or derivatives) are unallowable. The goal of this reform idea was to protect the government from the scenario where recipients were charging losses from financing arrangements to awards as direct costs, but not crediting gains when accrued.

Comments received in response to this reform were generally negative. Many institutions argued that they necessarily use these types of arrangements in order to balance legitimate investment portfolios that are part of institution-wide financial management plans, not

exclusively for management of Federal awards. Nonprofits operating internationally argued that these types of financing arrangements are necessary in order to hedge against risk of currency fluctuations.

OMB concurs with the observations in the comments, and notes that OMB guidance governing grants is not intended to govern how an institution manages its financial portfolio beyond the assets related to Federal awards. Further, we find that the cases where recipients are inappropriately charging losses directly to awards would already be unallowable under existing guidance and would result in an audit finding, so additional guidance is not needed to mitigate these risks. Based on comments received, OMB has not included language to this effect.

17. Providing non-profit organizations an example of the Certificate of Indirect Costs. Appendix V - Indirect (F&A) Costs Identification and Assignment, and Rate Determination for Non-Profit Organizations.

The ANPG discussed providing non-profit organizations an example of the required certification (Certificate of Indirect Costs) similar to the information that is already provided for state, local, and tribal governments. The goal of this reform idea would be to provide uniformity in

documentation requirements across different types of entities.

Though comments from the nonprofit community were generally favorable, the university community objected to this reform and argued that the certificate of indirect costs should be eliminated for all types of entities. They argued that there are other remedies available to the Federal government if an institution is alleged to have committed fraud, and the certification includes unfortunate language that diminishes the spirit of the collaboration between these organizations and the Federal government. Though OMB continues to see value in the certification of indirect costs by a senior official of the entity, this proposal modifies the language in the certification to be aligned with the language in the state/local/tribal certification, which articulates the certification using more positive language. This proposal is included in Appendix V- Indirect (F&A) Costs Identification and Assignment, and Rate Determination for Non-Profit Organizations, and provides slightly modified language for institutions of higher education in Appendix IV- Indirect (F&A) Costs Identification and Assignment, and Rate Determination for Institutions of Higher Education.

18. Providing non-profit organizations with an example of indirect cost proposal documentation requirements. (No language in proposed guidance)

The ANPG discussed providing for non-profit organizations an example of indirect cost proposal documentation requirements similar to the information provided for state, local, and tribal governments. The goal of this reform idea would be to provide uniformity in documentation requirements across different types of entities. Comments received in response to this idea as originally articulated were generally neutral. However, a broader principle of this reform effort has been to eliminate examples from the proposed guidance, as they can ultimately cause more confusion than clarity as over time they tend to be treated as the rule. Instead, OMB will provide guidance on documentation for justification of indirect cost rates that will more likely take the form of an instruction manual such as the one previously published by the Department of Labor (found at <http://www.dol.gov/oasam/programs/boc/costdeterminationguide/main.htm#toc>) rather than specific examples. As a result, this proposal does not provide such an example, and

further eliminates such examples for other types of entities.

19. Additional ideas for cost principles

In response to the ANPG, OMB received a number of suggestions for ways that existing guidance could be clarified beyond those articulated in the ANPG. OMB reviewed these and anticipates that clarifications made in the draft language in subchapter F may address many of them. Particular examples of requests that may have significant policy implications are:

A. Agency Exceptions to Use of Negotiated Cost Rates

(Section .616 Indirect (F&A) costs)). Many entities, in particular institutions of higher education, raised concern that Federal agencies do not always honor negotiated indirect cost rates, despite existing language in relevant circulars that appears to instruct them to do so. OMB recognizes that agencies do make exceptions to the general policy of reimbursing indirect costs at governmentwide negotiated rates. Further, OMB recognizes that the current system calculates indirect cost rates as an average across all Federal awards. As a result, for any given award, the actual associated indirect cost

will fall either above or below the negotiated rates, theoretically in even proportions.

In this proposal section .616 provides draft language to clarify the circumstances under which agencies may make exceptions to the negotiated rate. These include where exceptions are provided for in statute or regulation, or where the agency head has made a determination that the exception is important to the success of the program based on documented justification. Agency heads shall notify OMB of any approved deviations, so that OMB maintains a governmentwide view of the application of negotiated rates. OMB anticipates that programs with longstanding historical exceptions, such as NIH training grants, will continue within the new approval process. This stringent requirement for agency head approval should provide better transparency and understanding of these exceptions, and properly limit these exceptions to help ensure they are justified when they occur.

In addition, new language in section .502 Standards for Financial and Program Management provides that

voluntary committed cost sharing is not expected under Federal research proposals and is not to be used as a factor in the review of applications or proposals, except where otherwise required by statute. This is intended to ensure that research proposals are evaluated on their merit, and that cost sharing expectations where they exist are consistent for all applicants.

B. Clarifications of cost principles for information technology. OMB received several suggestions from the National Association of State Chief Information Officers (NASCIO) that requested clarification of the cost principles for information-technology systems. The first of these was a request that the item of cost for interest articulate that financing costs are allowable for intangible assets as well as capital assets such as large buildings. OMB has included proposed language to this effect in section .621 Selected Items of Cost. In addition, NASCIO requested that OMB clarify guidance on whether provisions in section .503 Property Standards (d) Equipment may apply to equipment for information technology systems which have been consolidated. In particular, NASCIO

requested including IT systems among the equipment which, when no longer needed by the Federal program for which it was originally purchased, may be used to support other Federally-funded activities. OMB has included proposed language to this effect in the above mentioned section.

C. Clarification of costs related to family-related leave and dependent care. Existing guidance has long allowed recipient institutions to establish their own documented institutional policies around fringe benefits and travel, and to fund external meetings and conferences provided they meet the conditions established by the relevant item of cost. However, OMB received suggestions from the American Association of University Women and other organizations indicating that because family-related leave and dependent care are not discussed specifically in OMB guidance, there may be confusion over the documentation required to establish their allowability. In response, we have included specific language in section .621, item C-11 Compensation - Fringe Benefits, C-32 Meetings and Conferences (external) and C-53 Travel Costs to clarify the requirements for documentation of these

costs. This language does not require adoption of any new practices, and best mitigates risk of abuse of these policies by clearly aligning them with the existing requirement that any such costs are only allowable to the extent they are reasonable and consistent with written institution-wide policy and practice.

D. Participant support costs. Existing guidance that applies only to nonprofit entities states that participant support costs are allowable when approved by the awarding agencies, and also notes that these costs are generally not included in calculations of modified total direct costs. This proposal would expand that language to all recipient entities in order to eliminate ambiguity in the guidance and to ensure appropriate Federal oversight and reimbursement for these types of expenses. Proposed language is in section .621, item C35 Participant Support Costs.

C. Reforms to Audit Requirements (Circulars A-133 and A-50) Subchapter G: Audit Requirements

This section discusses ideas for changes that would be made to the audit guidance that is contained in Circular A-133 on *Audits of States, Local Governments, and Non-Profit Organizations* and in Circular A-50 on *Audit Follow-up*. The following ideas for reform were discussed in the ANPG.

1. Concentrating audit resolution and oversight resources on higher dollar, higher risk awards. Sections .701 Audit Requirements and .719 Major Program Determinations

The ANPG discussed whether changing the Single Audit framework could enable agencies to focus their oversight and follow-up resources in the most efficient and effective way for targeting improper payments, waste, fraud, and abuse. The notice discussed options to raise the threshold for single audits from \$500,000 to \$1 million. Further, the notice discussed whether audits for entities expending between \$1 million-\$3 million could be streamlined to only two types of compliance requirements.

The goal of these reform ideas was to allow agencies to concentrate their audit oversight and follow-up resources more closely on areas of highest risk of waste, fraud, and abuse, consistent with EO 13520. For this purpose, OMB considers degree of risk as a combination of the likelihood

that there is an internal control weakness multiplied by the possible consequence in dollars if there is. This calculation recognizes that an entity spending the greatest amount of money with the greatest likelihood of an internal control weakness poses the greatest risk to integrity of Federal funds.

One of the questions OMB posed to commenters in the ANPG was the extent to which entities make use of the Single Audit in order to manage programs and provide oversight over subrecipients. The answer to this question in a great majority of responses was that entities do make use of the Single Audit as an important oversight tool, and if the threshold were significantly raised entities would have to make use of different tools to provide oversight over Federal funds. Entities who would fall below the raised threshold inquired about what types of oversight could replace the Single Audit if it were no longer in place.

OMB received significant feedback from the audit community (e.g. certified public accountants, state auditors, and their professional organizations) that argued against a streamlined audit for entities expending between \$1 million and \$3 million in Federal awards. This community argued that inconsistencies in the types of entities receiving

funds within a particular program would make it difficult to specify the one or two types of compliance requirements that would universally apply. Further, pass-through entities expressed concern that varying requirements significantly by program and size of entity would make it more administratively burdensome to oversee over subawards.

OMB also received several additional suggestions about how to re-configure the single audit coverage framework in order to best target risk. These suggestions included raising the threshold for determinations of major programs, changing the requirement for auditors to evaluate type B programs, raising the threshold for the amount of questioned costs, and requiring audited financial statements for all entities that fall below a new, higher single audit threshold.

As a result, this proposal contains the following changes in Subchapter G, Audit Requirements:

(A) Audit threshold. The threshold for the Single Audit Requirement would be raised from \$500,000 to \$750,000. This change would allow agencies to focus audit-follow-up resources on higher-risk entities. Further, this provides administrative burden relief to the roughly 5,000 non-Federal entities expending less than \$750,000 in Federal

awards while maintaining single audit coverage over more than 99 percent of the funds that are currently covered.

(B) Major Program Determination. This proposal includes changes to all four steps of the risk-based approach to focus on the areas of highest risk and reduce the number of major programs tested. Under the risk-based approach the auditor calculates a threshold (based on amount of Federal dollars expended) above which programs are designated "Type A" and below which they are "Type B"; and follows a prescribed process to assess program risk to identify which programs will be audited as major programs. The auditor uses the guidance in the Compliance Supplement to test major program requirements and provides opinion level audit assurance on each major program. (See section .719 Major Program Determination) The proposed changes to this process are as follows:

1. Increase the minimum threshold for a program to be Type A from \$300,000 to \$500,000 (but do not change the alternative three percent of total Federal awards expended). (Step 1)
2. Refocus the criteria for a Type-A program to qualify as high-risk. Revised criteria would result in a Type A

program being designated as high-risk only when in the most recent period the program failed to receive an unqualified opinion; had a material weakness in internal controls; or had questioned costs exceeding five percent of the program's expenditures. This change puts the focus of the risk determination on the most central questions of whether the program received a qualified opinion or had weak internal controls, as opposed to whether the program may have received any minor finding that may or may not have been essential to the financial integrity of the program. The requirement that a Type-A program be audited as major at least once every three years, regardless of whether it is high- or low-risk remains unchanged. (Step 2)

3. Reduce the number of high-risk Type-B programs that must be tested as major programs from at least one half to at least one fourth of the number of the low-risk Type A programs and allow the auditor to stop the Type-B program risk assessment process after this number of high risk Type-B programs are identified. (Steps 3 and 4)
4. Simplify the calculation to determine relatively small Type-B programs for which the auditor is not required to

perform a risk assessment from the current stepped approach to a flat 25 percent of the Type A/B threshold. The change allows more Type-B programs to be classified as relatively small. (Step 3)

5. Reduce the minimum coverage required under the percentage-of-coverage rule from the current 50 percent for a regular auditee and 25 percent for a low-risk auditee to at least 40 percent for a regular and 20 percent for a low-risk auditee. (Step 4)

These changes to the major program determination will result in more targeted audit coverage of programs with internal control weaknesses. They provide appropriate burden relief for non-Federal entities that materially comply as evidenced by an unqualified audit opinion, and no material weaknesses in internal controls or material questioned costs. Because large non-Federal entities (such as a larger state government) often have at least one audit finding in a program, under existing guidance, for these entities, almost all Type A programs may qualify as high-risk. The proposed changes provide an incentive for these non-Federal entities to focus on correcting the

deficiencies that indicate underlying weaknesses in internal controls.

(C) Questioned Costs. Increase the minimum threshold for reporting questioned costs from \$10,000 to \$25,000 to focus on the audit findings presenting the greatest risk. This will eliminate smaller audit findings which require the investment of follow-up resources yet are unlikely to indicate significant weaknesses in internal controls. (See section .717 Audit Findings)

In addition, to address questions about the required level of subrecipient oversight, OMB has consolidated and clarified relevant guidance on subrecipient monitoring requirements in section .501 Subrecipient Monitoring and Management.

If these reforms to the audit threshold were implemented, OMB would consider issuing further guidance about the transition to the GAGAS-only audit and the extent to which recipients with known weaknesses would be required to resolve them before being subject to it.

2. Streamlining the types of compliance requirements in the Circular A-133 Compliance Supplement. Some language in

Section .713 Responsibilities, but more to be added in
Single Audit Compliance Supplement.

The ANPG discussed streamlining the types of compliance requirements found in the OMB Circular A-133 Compliance Supplement. The notice discussed streamlining these requirements by targeting a subset for increased testing, larger sample sizes, or lower levels of materiality, while de-emphasizing others, with an exception allowing Federal agencies on a program-specific basis to place higher emphasis on those other specific types of requirements believed to prevent waste, fraud, or abuse.

The goal of this reform idea would be to refocus the Compliance Supplement to better target areas of risk, thereby reducing the audit burden on non-Federal entities and allowing agencies to concentrate their oversight and audit follow-up resources on the requirements targeting the highest risk of improper payments, waste, fraud, and abuse.

Comments on this section from the audit community pointed out that to specify the amount of testing done for a particular type of compliance requirement would be incredibly complex across programs, and would likely conflict with the generally accepted auditing standards, which require auditors to use their professional judgment

about the level of testing necessary for any particular entity. Moreover, recipients were concerned that the exception that allowed Federal agencies to add back requirements that they felt were necessary for the program would result in even more administrative burden.

One popular observation, particularly from state governments, was that in earlier iterations of discussions on these topics a reform idea was to eliminate certain types of compliance requirements altogether; many of these commenters argued that this elimination could be a clean way to reduce burden across programs.

As a result of this feedback, OMB proposes to limit the types of compliance requirements in the compliance supplement to the following group of key compliance requirements which, if violated, are most likely to result in improper payments, waste, fraud, or abuse. This approach is consistent with early recommendations received and OMB's October 2009 Single Audit Internal Control Project for American Recovery and Reinvestment Act (ARRA), which limited testing to the following basic types of compliance requirements.¹:

¹ The letter references are to the references used for the types of compliance requirements in the OMB Circular A-133 Compliance Supplement.

A. *Activities Allowed or Unallowed* and B. *Allowable Costs/Cost Principles* (combined) - The amounts reported as expenditures and claimed for matching will be tested for allowable activities and charges that were reasonable, allowable, and allocable under applicable OMB guidance and terms and conditions of award or grant agreement. Some review of H. *Period of Availability of Federal Funds* would likely be incorporated in a determination of allowability under this requirement. The *Matching* part of G. *Matching, Level of Effort, and Earmarking* would also be covered, since testing under this requirement will include a determination of whether costs claimed for matching are allowable, allocable, and reasonable. Documentation of appropriate matching claimed would still be reviewed under L. *Reporting*.

C. *Cash Management* -- The non-federal entity followed procedures to minimize the time elapsing between the transfer of funds from the U.S. Treasury, or pass-through entity, and their disbursement.

E. *Eligibility* -- The records show that those who received services or benefits, either directly or on behalf of someone else, were eligible to receive them: benefits were

provided in the right amount, to the right person, for the right purpose, and at the right time.

L. *Reporting* - Federal financial reports, performance reporting, claims for advances and reimbursement, and amounts claimed as matching are accurate and include all activity of the reporting period, are supported by applicable accounting records, and are fairly presented in accordance with program requirements. As noted above, this would include review of documentation of amount reported for matching.

M. *Subrecipient Monitoring* - The pass-through entity (1) made sub-awards only to eligible entities, (2) identified awards, compliance requirements, and payments to the subrecipient prior to disbursement, (3) monitored subrecipient activities to ensure subrecipient compliance, and (4) performed the audit resolution function (e.g., ensured proper audit submitted on time, followed up on audit findings, including issuance of a management decision, and ensuring that subrecipients took timely and appropriate corrective action).

N. *Special Tests and Provision* - Requirements that are unique to each federal program and are found in the laws, regulations, and the provisions of contract or grant agreements pertaining to the program which could have a direct and material effect on a major program.

The seven compliance requirements that would be eliminated from the compliance supplement would be D. *Davis Bacon*, F. *Equipment and Real Property Management*, the latter two components of G. *Matching, Level of Effort, and Earmarking*, H. *Period of Availability of Federal Funds* except where tested to verify allowable/unallowable costs, I. *Procurement and Suspension and Debarment*, J. *Program Income* and K. *Real Property Acquisition and Relocation Assistance*.

In order to accommodate programs where these requirements are essential to the oversight of the program and required by statute or regulation, OMB will consider requests from agencies to add one or more of these requirements back under special tests and provisions. Such requests for inclusion would only be accepted when compliance is required by statute or regulation, and when the federal agency (1) makes a strong case for how non-compliance with these types of requirements could result in increased risk

of improper payments, waste, fraud, or abuse; and (2) provides a targeted compliance supplement write-up identifying improper-payment risks and focusing audit tests to address these risks. If adopted, OMB will take appropriate steps to ensure consistency between programs for the same compliance requirement.

OMB believes that this approach will focus Single Audit resources where the risks to financial integrity are greatest and eliminate the more minute detail from audit reports that distracts agencies from identifying and addressing significant weaknesses in programs. This change is not reflected in the draft proposal but would be implemented through the first Compliance Supplement to be issued after the proposed change becomes final.

3. Strengthening the guidance on audit follow-up for Federal awarding agencies. Section .713 Responsibilities.

The ANPG discussed various policy options to strengthen audit follow-up at the Federal agency level. Ideas contemplated included:

- requiring agencies to designate a senior accountable agency official to oversee the audit resolution process;
- requiring agencies to implement audit-risk metrics including timeliness of report submission, number of audits that did not have an unqualified auditor opinion on major programs, and number of repeat audit findings;
- encouraging agencies to engage in cooperative audit resolution with recipients; and
- encouraging agencies to take a pro-active approach to resolving weaknesses and deficiencies, whether they are identified with single specific programs or cut across the systems of an audited recipient.

Further, to improve audit follow-up, the notice contemplated digitizing Single Audit reports into a searchable database to support analysis of audit results by Federal agencies and pass-through entities.

The goal of these reforms is to strengthen audit resolution policies to result in agencies taking a more pro-active and collaborative approach towards following-up on audit findings, which should result in a decrease in audit findings and program risk over time. Combined with the

reforms above to focus the Single Audit on the major programs and types of compliance requirements likely to result in the greatest risk of waste, fraud, and abuse, this reform would strengthen the oversight and response to those high-risk findings that were identified. As underlying programmatic weaknesses are resolved and repeat findings reduced, both recipients' and agencies' audit burdens would be lessened.

Comments received in response to these ideas were generally positive, and this proposal includes language on these ideas in section .713 Responsibilities. One additional suggestion OMB received was to consider making audit reports publicly available through the Federal Audit Clearinghouse. OMB acknowledges that making these reports public would reduce burden on the pass-through entities as they work to follow-up with subrecipients to obtain reports needed for oversight. OMB will work with the Federal Audit Clearinghouse to determine if privacy concerns over personally-identifiable information and confidential-business information can be overcome. One idea is that these concerns could be addressed by explicitly placing the responsibility on non-Federal entity uploading the reports to ensure that no such information is included. OMB has

included draft language in this proposal section. 713 Responsibilities to reflect the possibility that these concerns will be sufficiently resolved.

OMB will consider providing additional guidance on agency use of cooperative audit-resolution mechanisms and metrics to track audit effectiveness in order to ensure agencies are held accountable for improvements to use of the Single Audit process. OMB believes that taken together these steps will result in a more robust single audit framework providing strong oversight over high-risk programs, entities, and findings and providing incentives for prompt corrective action to strengthen the overall integrity of our Federal financial-assistance programs.

4. Reducing burden on pass-through entities and subrecipients by ensuring across-agency coordination.
Section .713 Responsibilities.

The ANPG discussed strengthening language that would reinforce cross-agency coordination of audits and audit follow-up.

The goal is to reduce redundancy and burden by making more explicit the existing requirement that the Federal cognizant or oversight agency coordinate audits or reviews

by other Federal awarding agencies that are made in addition to the Single Audit. This proposed change would not affect the ability of Inspectors General to conduct audit work as deemed necessary in accordance with the Inspector General Act of 1978, as amended.

This proposal includes language to this effect in section .713 Responsibilities, which, though not a change in policy, makes clear that it is the responsibility of the cognizant or oversight agency to coordinate audits or reviews by other Federal agencies that are made in addition to the Single Audit.

5. Reducing burdens on pass-through entities and subrecipients from audit follow-up. Section .713 Responsibilities.

The ANPG discussed the idea that for subrecipients receiving a majority of their awards directly from the Federal government, the Federal cognizant or oversight agency might be the most appropriate entity to conduct follow-up on audit findings that cut across multiple programs.

The goal of this reform is to eliminate duplicative audit follow-up work performed by a pass-through entity without

providing significant additional work to Federal agencies that already will be following up on these same audit findings, as well as to simplify the follow-up for the subrecipient.

Comments received in response to this reform were generally positive, though some commenters particularly in the university community argued that pass-through entities should not be at all responsible for conducting audit follow-up for subrecipients that receive a majority of their funds directly.

This proposal attempts to address this issue at both the Federal and pass-through level by making management decisions available through the Federal Audit Clearinghouse, on the possibility that privacy-related concerns articulated above can be resolved. This proposal articulates that the cognizant or oversight agency will provide management decisions for all findings in which it has funds directly implicated, and will make those management decisions publicly available so that other Federal awarding agencies and pass-through entities may decide to rely on them, or may decide to issue their own decisions, as appropriate. This should streamline the

audit-resolution process and result in relieved administrative burden both for the Federal awarding agencies and pass-through entities as well as for the subrecipient.

6. Additional ideas for audit requirements

In response to the ANPG, OMB received a number of additional suggestions for ways that existing guidance on audit requirements could be clarified. OMB reviewed these and anticipates that clarifications made in the draft language in Subchapter G- Audit Requirements will address many of them.

One additional idea for reform suggested by many in the Federal agency and audit community was to reduce the amount of time for audit submission from the current nine months down to three months or six months. OMB supports this idea, but notes that it will require changes to legislation to accomplish.

D. Additional suggestions outside of the scope of this proposed guidance:

In addition to the ideas discussed above, OMB received many ideas for reforms to Federal grant policies which have merit but are not properly addressed through changes to governmentwide guidance. Some of these ideas include better coordination of regulations that are applicable or have an impact on Federal grant; use of the Federal rule-making process for agency grants policies; improvements in data quality across systems that support the Federal grants community; looking at regulations governing electronic imaging for documents for both grants and contracts; facilitating better coordination, consistency, and transparency between indirect cost rate setting agencies; and improving the training available to Federal grants professionals. OMB is committed to continuing improvements in the policies, practices, and systems that support the Federal grants community under the continuing leadership of the COFAR. OMB and the COFAR will continue to work together to reach out to stakeholders to continue these discussions and to evaluate where further improvements may continue to be made.

Daniel I. Werfel, Controller

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