



Nonprofits and the New OMB Uniform Guidance Know Your Rights ... and How to Protect Them

The federal Office of Management and Budget (OMB) has issued new rules that require governments at all levels – local, state, and federal – that hire nonprofits to deliver services to reimburse those nonprofits for their reasonable indirect costs (sometimes mistakenly called “overhead” or “administrative” costs¹) when federal dollars are part of the funding stream. In addition, the OMB Uniform Guidance streamlines and clarifies cost allocation and other rules related to government grants and contracts, removing some areas of confusion and inconsistency while treating more of a nonprofit’s expenses as direct (reimbursable) costs.

Writing about the Uniform Guidance, the [Controller of OMB declared](#) that “this historic reform will transform the landscape ... for generations to come. Comptroller Mader noted that the Uniform Guidance will, among other things, “reduce the total volume of financial management regulations for Federal grants and other assistance by 75%” and relax “overly prescriptive and obsolete procedural requirements.” In particular, he stressed the importance of the policy reform of reimbursing nonprofits for their indirect costs, a necessary expense that “supports the fundamental operations of the organization.”

In a statement, the National Council of Nonprofits highlighted the significance to nonprofits of the OMB Uniform Guidance: “The final rules ... implementing the OMB Uniform Guidance represent the federal government’s official recognition that all governments entering into written agreements with nonprofits to deliver services to the public have an affirmative duty to pay their fair share of the costs that those nonprofits incur.”²

The rules apply to written agreements (whether called “contracts” or “grants”) signed after December 26, 2014, and may require changes in the accounting, procurement, audit, and contracting procedures within individual nonprofits and between these organizations and their government partners. The extent of the changes depends on whether the nonprofit already earns federal funds directly from a federal department/agency or instead from a “pass-through” entity using federal funds – typically a state or local government or sometimes another nonprofit. Each nonprofit needs to learn its rights and responsibilities under the Uniform Guidance and take positive steps to protect those rights. This paper identifies the major changes in the Uniform Guidance related to cost allocation rules and payment of indirect costs.³

¹ While the terms indirect, administrative, and overhead are often used synonymously, they are not the same in the context of the Uniform Guidance. Indirect costs refers to *organizational* expenses shared across programs, while administrative costs relate to the allowable costs of *program/grant* administration. *Overhead* is a more generic term that is not used in the Uniform Guidance.

² “It’s Up to Nonprofits and State and Local Governments to Turn the Promise of the OMB Uniform Guidance into Reality for Individuals, Communities Served, and Taxpayers,” [Statement of the National Council of Nonprofits](#), December 19, 2014.

³ For more information on the OMB Uniform Guidance, go to www.cfo.gov/cofar/ and www.councilofnonprofits.org.

Know Your Rights

Thanks to the OMB Uniform Guidance, **as a nonprofit you have the right ...**

To Reimbursement for More of Your Direct Costs

The OMB Uniform Guidance clarifies numerous cost allocation rules and specifies more costs that are reimbursable as *direct costs*. For instance, in certain circumstances, program administration (e.g., secretarial staff dedicated to a specific program) can be reported as direct, rather than as indirect, costs.

To Reimbursement for Your Indirect Costs

The Uniform Guidance expressly requires pass-through entities (typically states and local governments, as well as some larger nonprofits) using federal funds and all federal departments/agencies to reimburse a nonprofit for the reasonable indirect costs it incurs. Nonprofits that have never had a federally approved indirect cost rate can elect either the *de minimis* rate of 10 percent of their modified total direct costs (MTDC) or negotiate a higher rate in accordance with the federal cost principles. Nonprofits that have already negotiated a federal indirect cost rate must be paid that amount.⁴ Generally, the mandate to pay indirect costs applies to most federal grant funds.⁵ The mandate does not apply in cases where a *federal* statute expressly caps the rate at which indirect costs can be reimbursed.

Protect Your Rights

The OMB Uniform Guidance only offers a *promise* of better treatment of nonprofits providing services under programs funded in whole or in part by the federal government. Turning that promise into reality requires actions on the part of every nonprofit earning federal funds, either directly or indirectly. Here are things you can do to protect your rights and help create a culture of compliance and sustainability.

Cost Allocation Rules: Learn them, Follow them, Negotiate with them

By understanding what the cost allocation rules allow, and managing your costs accordingly, you have the right to secure reimbursement for more of your nonprofit's costs than formerly permitted. Nonprofits should invest in training programs to ensure that staff fully understand, comply with, and make certain your organization benefits from the new cost allocation rules. Turn to your state associations of nonprofits for trainings or referrals. Many foundations are committed to promoting nonprofit sustainability through this type of training and may be willing to provide support.

Protecting and Negotiating a Reasonable Indirect Cost Rate

The indirect cost mandate in the OMB Uniform Guidance means that governments using federal funds must reimburse your nonprofit for your reasonable indirect costs. Whether your organization

⁴ 2 C.F.R. §200.331(a)(4).

⁵ See 2 C.F.R. §200.101 for OMB's description of which programs and funding streams are not covered by the Uniform Guidance.

receives the 10 percent *de minimis* rate or a higher negotiated rate will depend on your knowledge of the rules and ability to accurately allocate costs. All nonprofits are entitled to request the opportunity to negotiate an indirect cost rate with pass-through entities using the federal standards.

Potential Assertions and Responses

Because the OMB Uniform Guidance is a major change in how the federal government is directing that its funds are to be used, it is possible – especially in the early stages of implementation – that nonprofit subrecipients will encounter challenges when seeking full compliance by federal and pass-through entities. The transition from longstanding practices to the new rules depends on the individual decisions and actions of tens of thousands of different federal, state, and local government and nonprofit employees who may not know all of the details of the new federal rules. Recognizing that the OMB Uniform Guidance is the law of the land, the following section identifies potential problem areas and suggested responses.

1. “We don’t pay for that” (be it indirect, administrative, or overhead costs).

Governmental entities for many years have “stretched” federal dollars by limiting payments to nonprofits under grants and contracts only to direct costs, saying “we don’t pay for indirect costs.”⁶ That assertion has essentially forced nonprofits to subsidize what the governments demanded but refused to pay for (e.g., accounting, facilities, administrative expenses). Unless there is a *federal* statutory exception, then federal agencies/departments as well as pass-through entities may no longer refuse to pay some or all of a nonprofit’s indirect costs. That is what the indirect cost mandate in the OMB Uniform Guidance is all about.

What OMB Says: The Uniform Guidance mandates that in addition to direct federal awards, “All pass-through entities must ... ensure that every subaward ... includes: An approved federally recognized indirect cost rate negotiated between the subrecipient and the Federal government or, if no such rate exists, either a rate negotiated between the pass-through entity and the subrecipient (in compliance with this part), or a *de minimis* indirect cost rate as defined in §200.414 Indirect (F&A) costs, paragraph (b) of this part.”⁷ As explained in the Frequently Asked Questions, “The cost principles are designed to provide that the Federal awards pay their fair share of the costs recognized under these principles.”⁸

What you can do: Insist that the government official put in writing the reason for not paying your indirect costs as required under the OMB Uniform Guidance. Then take the written refusal up the

⁶ In a nationwide study, the Urban Institute found that more than half (53 percent) of nonprofits with government contracts and grants reported that governments imposed limitations on reimbursement for indirect costs. Among those reporting such caps, the survey revealed that three out of four nonprofits (76 percent) were only able to recover an indirect cost rate of 10 percent or less; a quarter (24 percent) reported being paid zero. Sarah J. Pettijohn and Elizabeth T. Boris, with Carol J. De Vita and Saunji D. Fyffe, [Nonprofit-Government Contracts and Grants: Findings from the 2013 National Survey](#) (Urban Institute Center on Nonprofits and Philanthropy; Dec. 2013). Additional research reveals that the normal overhead rate for delivering services (for-profits and nonprofits) ranges from 25-35 percent. [Investing for Impact: Indirect Costs are Essential for Success](#) (National Council of Nonprofits; 2013) at page 8 and footnote 30.

⁷ 2 C.F.R. 200.331(a)(4).

⁸ FAQ.331-6.

chain of command – up to, and including the federal government department or agency that provided the grant money to the pass-through entity.

2. “The agreement isn’t the type covered by the OMB Uniform Guidance.”

Unless limited by a *federal* statute, the indirect cost mandate and other cost principles in the Uniform Guidance apply primarily to grants, cooperative agreements, cost reimbursement contracts, and fixed-price contracts. Further, some portions of the Uniform Guidance also pertain to certain entitlement funds. Whether out of past practice, local usage, lack of knowledge, or other reasons, some pass-through entities may incorrectly contend that the OMB Uniform Guidance does not apply to its agreement with the nonprofit even when federal money is being used.

What OMB Says: Anticipating this potential assertion, OMB made clear that the new rules are applicable based on the substance of the transaction, and not what the pass-through entity calls the agreement. Indeed, to avoid any confusion and resulting disruption in delivery of human services, the final revision of the Uniform Guidance added that the cost principles and the indirect cost mandate apply to “fixed-price contracts when there is a cost analysis or rate negotiation.”⁹ Given the extensive use of fixed-price contracts by pass-through entities with human services providers, the inclusion of this language in the Uniform Guidance essentially eliminates the need to clarify “is it a grant or a contract?”; the cost principles will apply if the funds originated as federal grants no matter what such agreements are labeled.

What you can do: Nonprofits should focus on the substance of their agreements so they can accurately determine the applicability of the Uniform Guidance and utilize the above citations if told that indirect costs do not apply to their agreement. If denied reimbursement, request a written explanation of the denial. That written explanation will provide the needed documentation to officially or unofficially appeal the decision.

3. “We demand that you waive your rights.”

In the past, some government employees have sought to avoid statutory and regulatory mandates by requiring nonprofits to forgo their rights, such as by demanding that the nonprofit sign a waiver before being awarded a contract or grant. This tactic is not allowed under the indirect cost mandate in the OMB Uniform Guidance.

What OMB Says: “If the subrecipient already has a negotiated [indirect cost] rate with the Federal government, the negotiated rate must be used. It also is not permissible for pass-through entities to force or entice a proposed subrecipient without a negotiated rate to accept less than the *de minimis* rate.”¹⁰

What you can do: Unless otherwise expressly authorized by federal law, a state or local government official may not require or encourage a nonprofit to waive its right to reimbursement for indirect costs. If presented with a waiver form to sign, nonprofits should first inform the pass-through official of the requirement to pay indirect costs under 2 C.R.R 200.331(a)(4) and the prohibition against

⁹ 2 C.F.R 200.101.

¹⁰ FAQ.331-6.

seeking to force or entice a nonprofit to forgo the *de minimis* rate under FAQ.331-6. The next step is to take the matter up with the official's superior, or with the federal department or agency that is providing the funding.

4. "This is not federal money so the Uniform Guidance doesn't apply."

Nonprofits in the past often have not known whether a grant or contract is funded in whole or in part with federal funds, as that information has often not been made available.

What OMB Says: The Uniform Guidance requires that pass-through entities disclose to nonprofit subrecipients that their subaward is made pursuant to a federal award to the pass-through entity and acknowledge the amount of federal funds involved.¹¹ This disclosure includes specifying the funding stream(s) being used. In response to a question about whether the rules still apply when state or local governments first use their own money and seek reimbursement after the fact, OMB stated: "any costs ultimately charged to a Federal award must comply with the terms and conditions of that Federal award, including the Uniform Guidance."¹²

What you can do: If a grant or contract agreement from a governmental entity does not include the federally required information cited above, the nonprofit should ask in writing what is the source of funds for the work that the nonprofit will perform. If doubt exists, the nonprofit should reiterate the requirements under the Uniform Guidance and the Frequently Asked Questions and request that a higher-ranking official intervene to provide full transparency about the source of funding.

5. "You can't include that as a direct cost."

In considering payments of indirect costs, pass-through entities are directing nonprofits how costs must be categorized.

What OMB Says: Pass-through entities do not have the authority to deviate from the dictates of the Uniform Guidance when it comes to application of the federal cost principles. The nonprofit organization determines whether a cost is categorized as direct or indirect based on its internal accounting procedures and federal cost principles. The Uniform Guidance explains that there is no universal rule for classifying certain costs as either direct or indirect (F&A) under every accounting system. A cost may be direct with respect to some specific service or function, but indirect with respect to the Federal award or other final cost objective. The one clear rule is that each item of cost incurred for the same purpose be treated consistently in like circumstances either as a direct or an indirect (F&A) cost in order to avoid possible double-charging of Federal awards.¹³

What you can do: Remind the pass-through entity that everyone is required to follow the federal cost principles and that the Uniform Guidance speaks directly to the fact that what is direct and indirect

¹¹ 2 C.F.R. 200-331(a)(1)

¹² FAQ.331-3.

¹³ 2 C.F.R. 100.412

varies by nonprofit, and that the diversity of practices should be respected as should the allocation method used in order to preserve the consistency in how costs are treated.¹⁴

6. "You have to prove your indirect costs are at least 10 percent of your modified total direct costs to receive the *de minimis* rate."

What OMB Says: In the preamble to the Uniform Guidance published in the federal register on December 26, 2013, the COFAR notes that the *de minimis* rate should remain conservative at 10% of modified total direct costs (MTDC) because it is an automatic rate without any review of actual costs.¹⁵

What you can do: Provide the citation or a copy of the language from the federal register that clearly states that the 10 percent *de minimis* rate does not require documentation of actual costs.

The information contained in this paper does not constitute legal advice. For more information, see the National Council of Nonprofits [webpage on the OMB Uniform Guidance](#).

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¹⁴ See 2 C.F.R. 200.414(b) *Diversity of nonprofit organizations*.

¹⁵ Federal Register/ Vol. 78, No. 248 / Thursday, December 26, 2013