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United States Department of State
and the Broadcasting Board of Governors
Office of Inspector General

Office of Audits

Independent Accountants' Report on the Application of Agreed-Upon
Procedures on Indirect Cost Rates Proposed by the
American Council of Learned Societies

Report Number AUD/CG-09-06, February 2009

L.F. Harris & Associates, CPA, P.A., performed the agreed-upon procedures under Department of State, Office of Inspector General, Contract No. S-AQMPD-04-D-0044, and by acceptance the report becomes a product of the Inspector General.



Harold W. Geisel
Acting Inspector General

2/24/09

Date

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Summary

At the request of the Department of State, Office of Inspector General (OIG), L.F. Harris & Associates, CPA, P.A., performed certain agreed-upon procedures to determine whether the indirect cost rates proposed by the American Council of Learned Societies for the fiscal years ended September 30, 2005, 2004, and 2003, complied with applicable regulations.

We found the Council's accounting system to be adequate for accumulating and reporting indirect costs under the provisions of Office of Management and Budget (OMB) Circulars A-122, codified at 2 CFR Part 230, *Cost Principles for Non-Profit Organizations*, and A-110, *Uniform Administrative Requirements for Grants and Agreements With Institutions of Higher Education, Hospitals, and Other Non-Profit Organizations*.

We took exception to the rates reported by the Council for the fiscal years ended September 30, 2005, 2004, and 2003, and we recommend that the Bureau of Administration, Office of Logistics Management, Office of Acquisitions Management, International Programs Division, accept and finalize the Council's indirect cost rates for the fiscal years specified at 10 percent of total direct program costs in accordance with the limit established under provisions of the grants.

Background

The Council is a private, not-for-profit federation of national scholarly organizations. The purpose of the Council is the advancement of humanistic studies in all fields of learning and the maintenance and strengthening of relations among national societies devoted to such studies. The Council is funded by grants from private foundations and corporations and federal grants from the National Endowment for the Humanities, the Department, and other federal entities. The Department, through the Bureau of Intelligence and Research, administers Title VIII grants.

The Title VIII Program seeks to build expertise on the countries of Eurasia and Central and East Europe. It does this by supporting national organizations in the United States for advanced research, language and graduate training, and other activities conducted domestically and overseas. Authority for this program is contained in the Research and Training for Eastern Europe and the Independent States of the Former Soviet Union Act of 1983, Pub. L. 98-164, 22 U.S.C. §§ 4501-4508, as amended.

The Department awarded Title VIII grants to the Council for the years specified as shown in Table 1.

Table 1. Grants to American Council of Learned Societies – FYs 2006, 2005, and 2004

Grant Number	Grant Period	Grant Amount
S-LMAQM-06-GR-159	09/01/2006–08/31/2009	\$ 498,000
S-LMAQM-05-GR-125	09/15/2005–08/31/2008	517,000
S-LMAQM-04-GR-143	09/01/2004–08/31/2007	500,000
	Total Awards	\$1,515,000

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The Department gave the Council permission to use provisional indirect rates based on projected financials. Provisional rates are temporary rates used for funding and billing indirect costs pending the establishment of final rates for a specified time period. The Title VIII grants specify that under the grants, the Council's indirect costs are limited to 10 percent of total direct program costs. The Title VIII grants also specify that the Council is subject to the requirements of OMB Circulars A-110; A-122; and A-133, *Audits of States, Local Governments, and Non-Profit Organizations*.

Purpose, Scope, and Methodology

Our primary purpose was to determine whether the Council's indirect cost rate structure for FYs 2005, 2004, and 2003 complied with applicable regulations. We conducted the testing and assessment at the Council's office in New York, New York, from December 4-8, 2006.

OMB Circular A-122 establishes principles and standards for determining costs for federal awards carried out through grants, cost-reimbursement contracts, and other agreements with not-for-profit organizations. The principles are for the purpose of cost determination and are designed to ensure that federal awards bear their fair share of costs.

The principles and standards of OMB Circular A-122 apply to both direct and indirect costs. A direct cost is a cost that can be identified specifically with a particular cost objective. Examples of direct costs include employee compensation and benefits, supplies, and travel. An indirect cost is a cost that cannot be identified with a single, final cost objective but that is identified with two or more final cost objectives, one or more of which benefit federal programs. Such costs should be combined into groups or pools and should be distributed to benefit final cost objectives in a manner that will produce an equitable result based on relative benefits derived.

We designed our approach to determine the Council's compliance with OMB Circular A-122, which describes selected cost items, allowable costs, and standard methodologies for calculating indirect cost rates for not-for-profit organizations. The purposes of OMB Circular A-122 are to

- ensure that the federal government bears its fair share of costs,
- identify allowable costs for determining the actual cost of federal programs, and
- establish policies and procedures for indirect cost allocation plans.

Our procedures included the following:

1. determining that charges to cost pools used in calculating indirect cost rates were mathematically accurate and supported by the grantee's accounting records and audited financial statements;
2. assessing the allowability and allocability of indirect costs by testing selected transactions to supporting documentation and inquiring about the nature and functions of activities included in the indirect cost pool;

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3. assessing the causal and beneficial relationship between indirect costs and cost activities;
4. analyzing the allowability and allocability of accounts that make up the Council's fringe benefit pool and calculating a recommended fringe benefit rate;
5. reviewing the general ledger to determine whether the grantee had income and credits and, if so, if they were credited to the indirect cost or fringe benefit pools as appropriate; and
6. inquiring about applicable fiscal year operations and assessing the impact of changes on the indirect cost rate structure.

Our approach to addressing the procedures was as follows:

1. We obtained an understanding of internal control over the subject matter of this engagement through inquiry and observation, the performance of an assessment of risk, and the testing of internal controls.
2. For direct costs, we determined whether the Council complied with the provisions of OMB Circular A-122 by
 - a. testing direct charges to federal awards for allowability and
 - b. verifying that unallowable costs that were determined to be direct costs were included in the allocation base for the purpose of computing an indirect cost rate.
3. We tested indirect costs to determine whether
 - a. the base used to distribute the approved allowable indirect cost was appropriate and reasonable and in accordance with the requirements of OMB Circular A-122;
 - b. the calculated indirect cost rate was
 - i. consistent with policies and procedures that apply uniformly to both federally funded and other activities of the Council and
 - ii. applied consistently to the proper allocation bases; and
 - c. the Council complied with the provisions of OMB Circular A-122 in that
 - i. charges to indirect cost pools were for allowable costs,
 - ii. the base used to distribute indirect costs included both allowable and unallowable costs, and
 - iii. the cost allocation methodology provides equitable and consistent allocation of indirect costs to benefiting awards or activities.

The scope of detail testing of individual accounts, internal controls, direct costs, indirect costs, regulation compliance, and other applicable records are a matter of judgment. Auditors cannot assume responsibility for fraud detection or prevention. Auditors are expected to maintain an alertness that will permit adequate inspection of the financial records as well as of

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the internal controls, internal accounting, and administrative controls. As such, the auditors were alert to the possibility of intentional wrongdoing, errors and omissions, inefficiency, waste, ineffectiveness, and conflicts of interest.

Results

Indirect Cost Rates

We found that the Council's accounting system was adequate to properly identify and segregate direct and indirect costs, as well as allowable and unallowable costs, for the fiscal years ended September 30, 2005, 2004, and 2003, under the provisions of OMB Circular A-122.

We took exception to the rates reported by the Council for the years specified and recommended the rates, as shown in Table 2, under the provisions in the Title VIII grants that limit indirect costs to 10 percent of total direct program costs.

Table 2. The Council's Proposed Indirect Cost Rates and Recommended Rates

Fiscal Year	Description	Council Proposed Rate	Auditor Computed Rate	Recommended Rate
2005	General and Administrative Overhead	9.1%	20.20%	10%
		27.3%	16%	10%
2004	General and Administrative Overhead	9.1%	18.38%	10%
		27.3%	15.59%	10%
2003	General and Administrative Overhead	9.1%	30.06%	10%
		27.3%	19.69%	10%

A listing of the indirect rates and supporting calculations for the indirect cost rates identified is in Attachment A.

Recommendation 1: We recommend that the Bureau of Administration, Office of Logistics Management, Office of Acquisitions Management, International Programs Division, accept and finalize the indirect cost rates of the American Council of Learned Societies for the fiscal years ended September 30, 2005, 2004, and 2003, at 10 percent of total direct program costs, as recommended by this report.



L.F. Harris & Associates, CPA, P.A.
Certified Public Accountants

INDEPENDENT ACCOUNTANTS' REPORT ON APPLYING AGREED-UPON PROCEDURES

U.S. Department of State
Office of Inspector General
Office of Audits
1700 North Moore Street
Arlington, VA 22209

We have performed certain agreed-upon procedures (the Procedures), as summarized in the Purpose, Scope and Methodology section of this report. The Procedures, which were agreed to by the Office of Inspector General, U.S. State Department, were performed solely to assist the Office of Inspector General, U.S. State Department in evaluating the Council's computations of their indirect cost rates in accordance with OMB Circular A-122 for the fiscal years ended September 30, 2005, 2004, and 2003.

The Council's management is responsible for compliance with those requirements. This agreed-upon procedures engagement was conducted in accordance with attestation standards established by the American Institute of Certified Public Accountants and guidance from the Office of Management and Budget. The sufficiency of these Procedures is solely the responsibility of those parties specified in this report. Consequently, we make no representation regarding the sufficiency of the Procedures as described in the Purpose, Scope and Methodology section of this report either for the purpose for which this report has been requested or for any other purpose. Our Test Procedures revealed three findings. The findings and the associated recommendations are presented in the "Results of Review" section of this report.

We were not engaged to, and did not perform an audit, the objective of which would be the expression of an opinion on the total costs claimed. Accordingly, we do not express such an opinion. Had we performed additional procedures, other matters might have come to our attention that would have been reported to you.

This report is intended solely for the use of the U.S. Department of State, Office of Inspector General, and should not be used by those who have not agreed to the Procedures, and taken responsibility for the sufficiency of the Procedures for their purposes.

A handwritten signature in black ink that reads "L.F. Harris & Associates". The signature is written in a cursive, flowing style.

L.F. Harris & Associates, CPA, P.A.
December 8, 2006

Attachment A – Supporting Schedules Page 1 of 3

American Council of Learned Societies Schedule of Indirect Costs Allowable and Indirect Cost Rates For the Year Ended September 30, 2005

Indirect Costs	Reference for Unallowed Costs*	Recorded Costs	Proposed Adjustments	Allowable Costs
Salaries and employee benefits		\$ 561,286	\$ -	\$ 561,286
Meetings and conferences	(a) (b) (c)	260,568	(146,516)	114,052
Office expense		138,459		138,459
Consultants/honoraria		72,316	-	72,316
Printing and publishing		32,723	-	32,723
Dues	(e) (b)	50,007	(16,502)	33,505
Other	(f)	1,475	(200)	1,275
Total Administrative Indirect Costs Allowable		\$ 1,116,834	\$ (163,218)	\$ 953,616
Interest Expense	(g)	\$ 260,406	\$ (4,063)	\$ 256,343
Depreciation and amortization		249,870		249,870
Rent and maintenance	(h)	92,135	48,782	140,917
Insurance		4,000		4,000
Total Overhead Indirect Costs Allowable		\$ 606,411	\$ 44,719	\$ 651,130
G&A Allocation Base:				
Total adjusted expenses (participant support costs)				\$ 3,859,313
Add: Unallowable activities				210,218
Add: Overhead expenses				651,130
Total Adjusted Direct Expenses				\$ 4,720,661
Overhead Allocation Base:				
Total adjusted expenses (participant support costs)				\$ 3,859,313
Add: Unallowable activities (includes \$47,000 of fund raising expenses)				210,218
Total Adjusted Direct Expenses				\$ 4,069,531
Indirect Rates Calculations:				
Administration: Total Administrative Indirect Costs				
Allowable/Total Adjusted Direct Expenses				20.20%
Overhead: Total Overhead Indirect Costs Allowable/Total				
Adjusted Direct Expenses				16.00%
Total				36.20%

*References explained at end of Attachment A.

Attachment A – Supporting Schedules Page 2 of 3

**American Council of Learned Societies
Schedule of Indirect Costs Allowable and Indirect Cost Rates
for the Year Ended September 30, 2004**

Indirect Costs	Reference for Unallowed Costs*	Recorded Costs	Proposed Adjustments	Allowable Costs
Salaries and employee benefits		\$ 544,687	\$ -	\$ 544,687
Meetings and conferences	(a) (b) (c)	236,163	(197,939)	38,224
Office expense		104,056	-	104,056
Travel		10,884	-	10,884
Consultants/honoraria		72,632	-	72,632
Printing and publishing		49,295	-	49,295
Dues	(e) (b)	37,162	(13,451)	23,711
Professional and other fees		35,000	-	35,000
Other	(f)	2,079	(200)	1,879
Total Administrative Indirect Costs Allowable		<u>\$ 1,091,958</u>	<u>\$ (211,590)</u>	<u>\$ 880,368</u>
Interest Expense	(g)	\$ 256,371	\$ (1,648)	\$ 254,723
Depreciation and amortization		253,909	-	253,909
Rent and maintenance	(h)	113,811	19,838	133,649
Insurance		4,000	-	4,000
Total Overhead Indirect Costs Allowable		<u>\$ 628,091</u>	<u>\$ 18,190</u>	<u>\$ 646,281</u>
G&A Allocation Base:				
Total adjusted expenses (participant support costs)				\$ 3,888,095
Add: Unallowable activities				256,590
Add: Overhead expenses				646,281
Total Adjusted Direct Expenses				<u>\$ 4,790,966</u>
Overhead Allocation Base:				
Total adjusted expenses (participant support costs)				\$ 3,888,095
Add: Unallowable activities (includes \$45,000 of fund raising expenses)				256,590
Total Adjusted Direct Expenses				<u>\$ 4,144,685</u>
Indirect Rates Calculations:				
Administration: Total Administrative Indirect Costs Allowable/Total Adjusted Direct Expenses				18.38%
Overhead: Total Overhead Indirect Costs Allowable/Total Adjusted Direct Expenses				15.59%
Total				<u>33.97%</u>

*References explained at end of Attachment A.

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Attachment A – Supporting Schedules Page 3 of 3

American Council of Learned Societies
Schedule of Indirect Costs Allowable and Indirect Cost Rates
for the Year Ended September 30, 2003

Indirect Costs	Reference for Unallowed Costs*	Recorded Costs	Proposed Adjustments	Allowable Costs
Salaries and employee benefits		\$ 856,956	\$ -	\$ 856,956
Meetings and conferences	(a) (b) (c)	296,769	(160,155)	136,614
Office expense		118,130	-	118,130
Travel		17,041	-	17,041
Consultants/honoraria	(d)	42,740	(40,000)	2,740
Printing and publishing		42,936	-	42,936
Dues	(e) (b)	50,680	(17,763)	32,917
Professional and other fees		37,466	-	37,466
Other	(f)	2,512	(200)	2,312
Total Administrative Indirect Costs Allowable		<u>\$ 1,465,230</u>	<u>\$ (218,118)</u>	<u>\$1,247,112</u>
Interest Expense	(g)	\$ 276,491	\$ (1,974)	\$ 274,517
Depreciation and amortization		249,660	-	249,660
Rent and maintenance	(h)	129,289	24,951	154,240
Insurance		4,000	-	4,000
Total Overhead Indirect Costs Allowable		<u>\$ 659,440</u>	<u>\$ 22,977</u>	<u>\$ 682,417</u>
G&A Allocation Base:				
Total adjusted expenses (participant support costs)				\$3,205,358
Add: Unallowable activities				261,118
Add: Overhead expenses				682,417
Total Adjusted Direct Expenses				<u>\$4,148,893</u>
Overhead Allocation Base:				
Total adjusted expenses (participant support costs)				\$3,205,358
Add: Unallowable activities (includes \$43,000 of fund raising expenses)				261,118
Total Adjusted Direct Expenses				<u>\$3,466,476</u>
Indirect Rates Calculations:				
Administration: Total Administrative Indirect Costs Allowable/Total Adjusted Direct Expenses				30.06%
Overhead: Total Overhead Indirect Costs Allowable/Total Adjusted Direct Expenses				19.69%
Total				<u>49.75%</u>

*References explained at end of Attachment A.

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References for Unallowed Costs in Attachment A

Reference Letter	Citation	Explanation
(a)	2 C.F.R. pt. 230 app. § A(A)(2)(g) (2009)	Inadequately supported meeting/conference/travel expenses are unallowable.
(b)	2 C.F.R. pt. 230 app. § B(14) (2009)	Costs of entertainment and social activities are unallowable.
(c)	2 C.F.R. pt. 230 app. § B(3) (2009)	Costs of alcoholic beverages are unallowable.
(d)	2 C.F.R. pt. 230 app. § B(42)(a)(3) (2009), (d)(1) (2009)	Relocation costs paid to new employees are limited to the employee's actual (or reasonably estimated) expenses. Funds paid to an employee for relocation are not discretionary and are limited to specific costs to include transportation, the costs of finding a new home, and temporary living quarters. Fees and costs associated with acquiring a new home are unallowable.
(e)	2 C.F.R. pt. 230 app. § B(30)(d) (2009)	Costs of membership in any country club or social or dining club or organization are unallowable.
(f)	2 C.F.R. pt. 230 app. § B(30)(d) (2009)	Costs of gifts are unallowable.
(g)	2 C.F.R. pt. 230 app. § B(23)(a)(6)(c) (2009)	Interest expense shall be reduced by an amount equal to imputed interest earnings on excess cash flow.
(h)	2 C.F.R. pt. 230 app. § B(43)(a) (2009)	Rental costs of buildings and equipment are allowable indirect expenses.

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