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Office of Management and Budget Releases New “Omni-Circular” Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards

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INTRODUCTION

On December 26, 2013, the Office of Management and Budget (“OMB”) released a comprehensive guidance that makes changes to the fragmented existing guidance on Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards.¹ This new guidance incorporates eight previous guidance circulars into one comprehensive policy guideline, commonly called the “Omni-Circular.”² Federal agencies are now tasked to develop implementing regulations based on OMB’s guidance that will affect how federal awards are administered to grantees, or non-federal entities (“NFEs”), defined by OMB to include state and local governments, Indian tribes, institutes of higher education, and nonprofit organizations. The goals of the new guidance are threefold: to maximize uniformity for federal awards among all agencies granting awards and NFEs receiving awards; to remove duplicative and conflicting requirements in order to increase efficiency and decrease administrative burden; and to increase oversight of federal awards to reduce the risk of waste, fraud, and abuse.

BACKGROUND

OMB’s new guidance was created in response to two directives issued by President Obama in 2009 and 2011. These directives required OMB to reduce regulatory and administrative burdens and redirect resources to services that are essential to achieving better outcomes at lower cost and to strengthen accountability by “intensifying efforts to eliminate payment error, waste, fraud, and abuse” in federal programs.³ Accordingly, in October 2011, OMB created the interagency Council on Financial Assistance Reform (the “COFAR”). Comprising representatives from the largest federal grant-making agencies, COFAR led reform efforts by

¹ 2 C.F.R §200.

² This final guidance supersedes and streamlines requirements from OMB Circulars A-21, A-87, A-110, A-122, A-89, A-102, and A-133; and the guidance in Circular A-50 on Single Audit Act follow-up.

³ February 28, 2011, Presidential 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>); Executive Order 13520 on Reducing Improper Payments (74 FR 62201; November 25, 2009; <http://www.gpo.gov/fdsys/pkg/FR-2009-11-25/pdf/E9-28493.pdf>).

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engaging with the federal and nonfederal financial assistance community over two years to draft the new guidelines with robust stakeholder input.⁴

Agencies have six months from the date of publication to submit implementing regulations to OMB. Nonfederal agencies will be required to comply with the new requirements once the implementing regulations are in effect, which will occur by December 26, 2014. The guidance will apply to audits in the fiscal year beginning after December 26, 2014. By requiring federal agencies to implement this guidance in unison, OMB seeks to provide NFEs receiving grants funding with a predictable, transparent, and consistent implementation schedule. Notably, the guidance attempts to create maximum uniformity among federal awards, but it does not currently incorporate the Cost Principles for Hospitals in the Department of Health and Human Services regulations.

OVERVIEW OF KEY POLICY CHANGES

A summary of some of the key policy changes and goals for federal awards and cooperative agreements in the OMB’s new Omni-Circular are highlighted below.

Eliminate Duplicative and Conflicting Guidance

As previously noted, a major goal of combining the eight guidance circulars into one comprehensive policy guide is to eliminate duplicative and conflicting guidance and to reduce administrative burdens on NFEs receiving federal awards. Specifically, the changes in the Omni-Circular eliminate the duplicative and conflicting guidance of the three current cost principles Circulars—A-21 for educational institutions; A-87 for state, local, and tribal governments; and A-122 for nonprofit organizations. COFAR also considered adding hospital cost principles to the Omni-Circular, but after much deliberation decided that to do so would require much further analysis and would be an exercise better suited to a separate project.

With the goal of creating uniformity among federal awards, the guidance makes clear that federal awarding agencies generally must not impose additional or inconsistent requirements for federal awards. Exceptions will be made if the requirement is based on federal statute, regulation, or Executive Order, or if approval is granted by OMB, which is only expected to occur in rare circumstances. Nevertheless, no exceptions will be allowed from any of the audit requirements (discussed below). While the guidance also outlines the applicability of each section to the types of federal awards, the awarding agency will state the relevant requirements directly in the terms and conditions of the federal awards. Accordingly, a recipient of grants funding will not need to decide which sections they will be required to follow.

Focus on Performance Over Compliance

As with previous awards, federal awarding agencies are still required to determine the appropriate award instrument in accordance with the Grant and Cooperative Agreement Act

⁴ COFAR is composed of the OMB Controller and senior policy officials from the National Science Foundation and the Departments of Agriculture, Education, Energy, Health and Human Services, Homeland Security, Housing and Urban Development, Labor, and Transportation.

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of 1978.⁵ However, the guidelines incorporate new coverage about a type of award called a fixed-amount award. Specifically, fixed-amount award payments are based on meeting specific requirements milestones, and accountability is based on performance and results. The goal of the coverage for fixed-amount awards is to minimize compliance requirements in favor of increased focus on meeting performance milestones. The award is negotiated using cost principles as a guide; so while there is a review of the costs up front, there is no government review of the actual costs incurred. For this reason, in order to ensure the grant is used for its original purpose, significant changes (i.e., principal investigator, project partner, or scope of the project) must receive prior written approval by the awarding agency. Agencies such as the National Science Foundation and the Department of Housing and Urban Development have already been successful at implementing this type of agreement.

The Omni-Circular also strengthens requirements for NFEs to maintain high standards for internal controls over their salaries and wages and allows for additional flexibility in how entities implement processes to meet those standards. In addition, it mandates that federal agencies approve alternative methods of accounting for salaries and wages based upon achievement of performance outcomes including, in approved instances, where funding from multiple programs is “blended” or “braided” to more efficiently achieve combined outcomes.

The Omni-Circular further raises the threshold for institutes of higher education to comply with cost accounting standards from \$25 million to \$50 million to match the threshold in the federal acquisition regulations. The process for federal agency review of changes in accounting practice is newly streamlined to reduce the risk of noncompliance, thus reducing audit findings. NFEs are to submit their modifications in accounting practice six months before implementing a change. They may proceed with the implementation if they receive no extension of the review period, or any indication of concern from the federal agency.

Encourage Efficient Use of Information Technology and Shared Services

The Omni-Circular includes an explicit requirement that NFEs must safeguard protected personally identifiable information for federal awards. This applies, for example, to the required posting of Single Audit Reports on the Internet, which must not contain any protected personally identifiable information.

Additionally, while coverage related to property standards is largely based on the requirements previously included in Circular A-110, there is a major exception with regard to equipment. While states have always been required to use, manage, and dispose of equipment acquired under a federal award in accordance with state laws and procedures, the Omni-Circular specifies that other NFEs must now follow the requirements as well. The guidance also creates more flexible standards for treatment of technology-related costs, by including all tangible personal property below a \$5,000 threshold in the less stringent definition of supplies instead of treating it as equipment.

In an effort to promote cost-effective use of shared services, the guidance encourages NFEs to enter into state and local intergovernmental agreements or inter-entity agreements if possible for procurement or use of common or shared goods and services. Additionally,

⁵ See 31 U.S.C. §6301.

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NFEs are encouraged to use federal excess and surplus property instead of purchasing new equipment and property when possible, and to reduce project costs.

Provide for Consistent and Transparent Treatment of Costs

The new Omni-Circular makes clear the applicability of the new guidance on cost principles to various kinds of assistance. Loans, scholarships, fellowships, institutes of higher education where capitation awards have been made, fixed-amount awards, and hospitals are specifically excluded from the cost principles.

A notable improvement from the previous guidances is the change to the requirements for prior written approvals. The new language on prior approvals pulls together in one section a comprehensive list of the 22 circumstances under which NFEs should seek prior approval from the federal awarding agency. This list includes revisions of budget or program plans, direct charging of administrative costs, and marketing costs.

The new Omni-Circular also makes the application of cost principles more consistent across federal awards and seeks to update policies on direct and indirect costs, in particular. For example, the guidance clarifies the circumstances under which it is allowable to charge administrative support costs as direct costs. This language was added to address a much-maligned inconsistency in the definition of “direct costs,” which required NFEs to charge administrative costs indirectly but otherwise provided that any costs may be charged directly when they can be specifically allocated to one award regardless of what activities they support. Under the former guidance, therefore, an NFE might be unsure of whether or not it was in compliance in charging an administrative cost, directly allocable to one award, as a direct cost. The new language eliminates this ambiguity: such costs are allowable when they are included in the approved budget or have prior approval by the federal awarding agency.

A new 10% de minimis indirect cost rate is now available to NFEs that have never received a negotiated indirect cost rate. This rate of 10% of modified total direct costs may be used indefinitely. If elected, the NFE must use the de minimis rate on all federal awards until it negotiates an approved rate with the federal agency supporting the award.

NFEs that do have a federally negotiated indirect cost rate may now apply for a onetime extension of up to four years without further negotiation, subject to the approval of the negotiating federal agency. If approved, the entity may not renegotiate its rate until the extension period ends. COFAR specifically notes that the extension may be “up to” four years, so this may include shorter extensions, subject to review by the federal agency for indirect costs.

Limit Allowable Costs to Make Best Use of Federal Resources

Certain limits on costs remain substantively the same between previous guidance on cost principles and the Omni-Circular. For example, the draft guidance received many comments urging COFAR to retain cost principles relating to advertising and public relations that allow costs of advertising, program outreach, and other specific fees that are necessary to meet the requirements of NFEs’ federal awards. In response to these requests, COFAR maintained the current policy on this issue.

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Some commenters were also concerned that the new Omni-Circular disallowed previously allowable costs for documented advisory council costs that benefited the federal award. Again under the new language, advisory council costs are still allowable if authorized by statute or with prior approval from the federal awarding agency.

Other notable changes are new and limit allowable costs. For example, costs incurred by an NFE to recover improper payments are allowable as either direct or indirect costs, as appropriate. Allowable conference spending is addressed in a new way and requires conference hosts or sponsors to exercise discretion and judgment in ensuring that conference costs are appropriate, necessary, and managed in a manner that minimizes costs to the federal award.

In the past, costs to improve employee morale were allowable even though those costs that were “entertainment” costs were not allowable. The previous language created a gray area susceptible to waste, fraud, or abuse. The new language is closely tailored and explains that costs incurred in accordance with the NFE’s documented policies for the improvement of working conditions, employer-employee relations, employee health, and employee performance are allowable. The Omni-Circular further clarifies that entertainment costs are unallowable unless those costs have a programmatic purpose and are authorized in the approved budget for the federal award, or those costs have prior written approval from the federal awarding agency.

The limits on idle facilities and idle capacity have also been updated. Commenters urged that the proposed one-year limit did not take into account that multiyear projects may require more flexibility. Under the Omni-Circular, the costs to maintain idle facilities are allowable for a reasonable period of time, ordinarily not to exceed one year, when they are necessary to fluctuations in workload, such as those that may be typical of developing shared service arrangements.

Finally, the Omni-Circular extends the policy on allowing organization costs to all NFEs under the cost principles, not just nonprofit organizations. Costs such as incorporation fees; broker fees; and fees to promoters, organizers or management consultants, attorneys, accountants, or investment counselors in connection with the establishment or reorganization of the organization are unallowable without federal awarding agency approval.

Set Standard Business Processes

For competitive grants and cooperative agreements, federal awarding agencies must announce specific funding opportunities by posting a public notice on the OMB-designated government-wide website.⁶ Agencies will now be required to provide enough information in the initial notice to allow potential applicants to determine eligibility at the outset, prior to viewing the full funding opportunity. The Omni-Circular specifies a set of six data elements that must be included in the public notice, including important dates and compliance deadlines. Although previous circulars have established the information an agency is required to provide to potential applicants, the Omni-Circular seeks to provide some commonality among how agencies develop the full-funding documents to ease navigation for potential applicants. Finally, the Omni-Circular establishes minimum time frames in which

⁶ See www.grants.gov.

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federal awarding agencies must generally make all funding opportunities available for application. The requirements state that a funding opportunity should generally be available for at least 60 days and, except in unusual circumstances, no opportunity should be available for less than 30 days.

Once an NFE receives a federal award, the federal awarding agency must include a set of 15 data elements in the award notice. Federal awarding agencies must also include an indication of the timing and scope of expected performance as related to the outcomes intended to be achieved. In some instances, such as discretionary research awards, this may be limited to submission of technical performance reports. The federal awarding agencies are required to provide recipients with clear performance goals, indicators, and milestones. Notably, this requirement does not apply to the research community if there is already a standard OMB-approved information collection for performance, such as the Research Performance Progress Report.

Encourage Nonfederal Entities to Have Family-Friendly Policies

In drafting the Omni-Circular, COFAR took seriously the goal of encouraging NFEs to help their employees balance responsibilities to both their families and the federal award. For example, guidance on cost principles for fringe benefits lists family-related leave among the examples of the types of leave that may be allowed according to the NFE’s consistently applied written policies.

In addition, the guidance on conferences encourages NFEs to have family-friendly policies allowing the hosts of conferences to defray the costs of identifying (but not providing) locally available dependent and child care resources. Relatedly, a separate provision provides that temporary dependent care costs that result directly from travel to conferences are allowable, under specific and limited circumstances.

Strengthening Oversight

Several provisions seek to strengthen oversight in the revised administrative requirements. Federal awarding agencies must establish conflict-of-interest policies for their federal awards. This is an important change because there are currently variances in the types and frequency of notifications that must be made. Some agencies already have conflict-of-interest requirements in place, and those requirements will continue to apply. Agencies that do not have existing conflict-of-interest policies will be required to establish such policies.

The Omni-Circular requires NFEs to disclose in writing any potential conflict of interest to the federal awarding agency in accordance with the federal agency’s policy. NFEs must maintain written standards of conduct covering conflicts of interest and governing the performance of its employees engaged in the selection, award, and administration of contracts. A new provision requires NFEs to maintain written standards of conduct covering organizational conflicts of interest if the entity has a parent, affiliate, or subsidiary organization that is not a state or local government or an Indian tribe. Additionally, NFEs receiving federal awards must disclose all violations of federal criminal law involving fraud, bribery, or gratuity violations potentially affecting the federal award.

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New disclosure requirements also require federal awarding agencies to design and execute a merit review process for applications for competitive grants or cooperative agreements. In addition, federal awarding agencies must establish a framework for evaluating the risks posed by applicants prior to receipt of a federal award. Although not required, data points that may be considered by federal awarding agencies include financial stability, quality of management systems, history of performance, reports and findings from audits, and applicants' ability to effectively implement statutory, regulatory, or other requirements. Federal agencies may apply special conditions on entities receiving grants that correspond to the degree of risk determined by the agency.

Other provisions seek to strengthen oversight of federal awards with regard to internal controls for NFEs. Required certifications must be signed by an organization official who can legally bind the NFE. When annual fiscal reports or vouchers requesting payment under an award are requested, the signatory official certifies the reports to be accurate and true, understanding that there are potential penalties under the False Claims Act.

Target Audit Requirements to Reduce Risk of Waste, Fraud, and Abuse

The current audit requirements found in Circular A-133 have been replaced in the new Omni-Circular. COFAR took the approach that below a certain federal award dollar amount, the Single Audit process is not cost-effective. As a result, the Omni-Circular adjusts the scope of the Single Audit requirements to strengthen oversight of programs that are audited, while at the same time focusing audits on NFEs where there is the greatest risk of waste, fraud, and abuse. To this end, the most important change is the audit threshold increase from \$500,000 to \$750,000. This increase relieves the audit burden on approximately 5,000 NFEs that are spending relatively small amounts of federal awards, while at the same time maintaining oversight over 99.7% of the dollars currently subject to Single Audit. Other changes to the determination of Major Programs also reinforce this risk-based approach by focusing audits on the areas with internal control deficiencies that have been identified as material weaknesses.

In addition, Single Audit Reports must now be posted online with safeguards for personally identifiable information. This change increases transparency in the audit process.

Although these represent significant changes, the basic structure of the single audit process has not changed, since the new requirements are still grounded in the Single Audit Act Amendments of 1996.⁷ Any changes to audit requirements guidance had to be consistent with the requirements of that legislation.

⁷ See 31 U.S.C. §7501, *et seq.*

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CONCLUSION

OMB’s new Omni-Circular creates an inclusive framework for delivery and administration of federal grants funding. NFEs receiving federal awards will be significantly impacted by this new guidance, which incorporates eight previous guidance circulars into one comprehensive guide. Federal agencies are required to develop implementing regulations, and NFEs receiving federal grants will be subject to compliance standards once these regulations are in effect, which will occur no later than December 26, 2014.

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