

COST ALLOCATION PLANNING

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The basic premise behind cost allocation and cost allocation planning is that each program or funding stream should be paying its fair share of the costs for the provision of services. When Head Start and Early Head Start programs have more than one funding source and use these funds for the provision of services, there must be a way to demonstrate that each program accepts its appropriate share of the costs.

If an agency receives funds from two or more sources, which could be federal, state, local, and/or private funds, there exists a potential for cost allocation. If the agency were to share common space that was not covered by some other costing mechanism, then this common space should be cost allocated. That is, the space should be portioned out or allocated and charged to the multiple funding streams. The same would hold true if, instead of space, the cost item was staff or equipment, etc. The method by which this allocation takes place, based upon written formulas and self developed rules, is the cost allocation plan.

Despite the fact that the OMB Circulars do not specifically call for a cost allocation plan for programs like Head Start, the OMB Circulars do require that the costs of shared resources be allocated fairly. This allocation is reviewed as part of each grantee's Federal Review. As the Office of Head Start tells us on the Early Childhood Learning and Knowledge Center (ECLKC), *"To document to auditors and Federal reviewers that costs have been properly allocated, some written account or plan is strongly recommended. Grantee agencies are encouraged to discuss a proposed cost allocation plan with the ACF grants officer and the auditor who performs the required annual audit."* The Office of Head Start also reminds us that *"for purposes of cost allocation in Head Start grantee agencies, cost allocation refers to the allocation of costs to various sources of funding, not to accounting categories."*

Programs should be mindful that cost allocation methods do not have to be complex and that Occam's razor suggests the simplest solution is usually the most useful. The stipulation, to divide the costs of shared assets, may be met by using common sense methods to guarantee that each program is paying its fair share of the cost. The basis for cost allocation should be tied to the function in question. For administrators, the basis might be a percentage of time spent in service to each program. Teachers could be allocated based upon a breakdown of the number of children served by each funding stream. Space costs could be allocated based upon square footage occupied by each program within the agency.

As can be seen, there are differing ways to allocate the costs. Many multi-funded agencies will have several options for allocating the costs and will depend on the cost center in question. This collection of the different ways that cost center expenses are allocated is the cost allocation plan for the agency. The Office of Head Start reminds us that *"general schemes that can be applied to large portions of the agency's budget and still fairly allocate shared costs are preferable to complex detailed schemes."*

Some typical bases include:

- Number of employees
- Amount of expenses
- Number of children
- Square Footage

The steps in cost allocation are:

1. Clearly define what is to be allocated and what may be directly billed to a program. Directly billed items do not have to be allocated.
2. Develop bases for allocation. Different bases can be used for different cost categories.
3. Allocate and record in accounting records.
4. Review allocation and bases to actual and correct if needed.

A word of warning on determining how to allocate the costs... Budget share is never the appropriate basis for the allocation. In other words, using budget share or "Head Start has the largest budget, so Head Start should pay the largest share of costs" is not acceptable. The share of the expense is determined by the cost allocation plan, not by program's percentage of the agency's budget.

There is no regulation indicating how frequently the cost allocation plan should be reviewed within the year, but it appears that the standard convention is quarterly. There is no single way to develop the plan. The cost allocation plan needs to make sense for the given situation being mindful that all programs within an agency are expected to pay their fair share of the expenses. By fair share, it is meant that the costs borne are proportional to the benefits received.

By way of conclusion, T/TAS has provided a brief checklist for cost allocation plans below:

Item	Yes	No
Is the cost allocation plan written?		
Does the cost allocation plan list the sources of revenue for the service to be cost allocated?		
Are the sources of revenue supported by historical information or estimated levels?		
Does the cost allocation plan explain how the costs are to be apportioned?		
Does the cost allocation plan provide a description of how expenditures within the major cost categories will be allocated and recorded in the grantee agency's accounting system?		
Does the cost allocation plan indicate how frequently it will be reviewed to ensure the assumptions are correct or otherwise need to be modified?		
Has the cost allocation plan been reviewed based on the self-determined timeline?		
Can the agency document the review of the cost allocation plan by staff members?		

A publication of
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