

Indirect FAQ

Introduction

WDFW has restructured our indirect rate because we realized several functions that support all agency work, including contracts, had not been included in our rate. The higher rate reflects the true costs of the work the agency performs as your agent.

Note on Terminology

Indirect applies to our receivable agreements – where we perform work on behalf of others through grants, contracts, or inter-agency agreements. We often refer to these as “contracts” for simplicity’s sake. This document uses “contracts”, “receivable agreements” and “agreements” interchangeably. However, the word “contracts” refers only to receivable contracts (where we receive funding). It does not refer to payable contracts (where we pay other for good or services).

Indirect Basics

1. What is indirect?

We apply an indirect rate to work we perform that is funded through contracts, grants and inter-agency agreements. The indirect rate is a tool that allows us to have these agreements pay for their proportionate share of the administrative support they use. The indirect rate covers costs that cannot be attributed to specific projects or that are more conveniently managed through the indirect rate process. For example, rather than having each payroll staff member track the few minutes they spend processing individual timesheets from each of the 1,000 specific agreements we have, we roll payroll costs together and the indirect rate recovers a small piece from each agreement.

2. What’s included in indirect?

The rate includes costs necessary to perform contracted work that is not specified in the statement of work. The rate recovers costs from tasks not directly linked to work products, but necessary to perform the work. Some costs are in Business Services, like payroll, IT and HR support. Indirect also includes some overhead costs, such as lease costs for our larger offices and computers. (Facility costs for smaller, contract-funded, single-purpose offices are typically direct costs.) Lastly, it includes administrative support within the resource programs, including senior managers, budget, contracts, and other administrative staff.

3. So all administrative costs are paid by our federal and local awards?

No. All administrative costs are included in our indirect rate calculation process, but the rate is designed so that all fund sources pay their fair share of support costs. Contracts, grants and inter-agency agreements fund about 46% of agency non-administrative staff, and indirect earned from those awards funds about 46% of agency-wide administrative costs. State funds support the remaining 54% of administrative functions and agency staff.

4. How is the indirect rate calculated?

The indirect rate is the ratio of support costs to project costs. An indirect rate of 25% means that, for every dollar of direct costs, there is an associated set of 25 cents of costs within the agency that are supporting that project.

Understanding the Current Indirect Rate Change

5. Why are we making any changes?

WDFW has not been recovering the true costs of our contract, grant and inter-agency agreement work, as required under state law. We had a number of agency support functions that were not included in the model, including positions like agency rules coordinator or program fleet managers. These positions are providing indirect support to all agency staff and to contractual work. By excluding them, we were not charging the true cost of the services we provide. This means our other fund sources, such as the state wildlife account and state general fund, were providing financial support to these contracts, grants and inter-agency agreements. Consequently, hunting or fishing license revenues were helping the federal or local governments get a discount when they contracted for our services.

6. Who changed the rate, and through what process?

WDFW has had an unpredictable rate over the last few years, with its indirect rate dropping from around 28% to as low as 20%. We started from scratch and rebuilt the entire model based upon accounting standards and the federal indirect principles, trying to create a more stable rate environment. A cross-program team reviewed the federal principles and our methodology. The group agreed to apply a standard set of criteria across all agency programs. We re-evaluated the appropriate program support and supervisory positions that should be included in the model. We also corrected factors in the model that could have resulted in over-billing and changed some direct costs to indirect costs to improve consistency.

7. What's the new rate going to be?

Our current indirect rate for Fiscal Year 2012 (FY12) is 23.51%. Our *proposed* core rate for FY13 is 27.36%, with the increase coming from a more thorough review of support functions. In the past, the Department of Interior has directed us to recover extra indirect when our rate has increased, as the higher rate means we were not recovering enough indirect before. They could ask us to charge as much as 31.38% to recover more indirect. However, WDFW has decided to phase in the recovery so our rate does not spike so much. We will set the rate at one percent above our core rate, and offset past under-recovery over the next four years or so. **For planning purposes, staff should assume a 28.36% indirect rate for FY13.**

8. Why is it necessary to recover funds from previous awards?

It is helpful to consider the federal government's perspective on this issue. A few years ago, they determined we had over-charged indirect on all of our awards. They therefore lowered our indirect rate until they had calculated that we had "repaid" our "debt". Basically, we had over-charged them in the past, so they would underpay us now to balance it out. The current situation is the opposite: we

had under-billed our receivable agreements, and now we will over-bill to compensate. This will restore funding to the hunters, anglers and general tax-payers whose license fees or tax dollars had been used to cover the lower indirect recovery. The goal is to be fair and not overcharge any group.

9. Is WDFW adding more administration using the higher rate?

No. Administrative positions will remain the same. The revised indirect rate includes administrative support that was not included in the past rate, ensuring that the costs of staff who support contractual work are recovered. In the past, the lower indirect rate resulted in state funds, including hunting and fishing license revenue, being used to help pay for support work on contracts, grants and inter-agency projects. The new rate will ensure we charge for the true costs of our work, and do not draw upon other funds.

10. How does the agency use earned indirect?

Earned indirect represents recovery of support functions that make the contractual work possible. WDFW builds its budget assuming we will earn a certain level of indirect. As programs perform contracted work, we bill the contracts to recover our costs. The earned indirect is then distributed to programs based upon the support services they provide. Essentially, every program starts the biennium with a large deficit for its support functions. As WDFW performs contractual work, the earned indirect fills that hole.

11. What does the agency do with earned indirect if it is higher than initial estimates for the biennium?

After years of difficult budgets, the agency has very limited margin for error. The agency has structural deficits in several IT, facility and unemployment costs, and manages its budget very carefully to cover those costs. If we earn more indirect than expected, it can help cover some of these unbudgeted expenditures.

Timing

12. When does the new rate go into effect?

The new rate will go into effect on July 1, 2012, and applies to all work conducted in FY13. All new awards for this period would apply the new rate. Awards that were signed in FY12 under the 23.51% indirect rate will also be affected beginning July 1. The contract does not need to be amended for the new rate to go into effect.

13. Will the new rate apply to existing agreements?

Yes. Generally, the new rate applies to all agreements for all work performed during Fiscal Year 13 (July 1, 2012 – June 30, 2013). We will use the new rate as we bill others for our services. Naturally, awards with capped indirect rates would be unaffected.

14. When will we know what the new rate is?

We sent in a proposal in January, but have not yet heard from the Department of Interior. We hope to know the new rate before the new fiscal year begins on July 1. The rate will be effective July 1, regardless of when the new rate is approved by the federal government.

Rate Comparison and Analysis

15. How does WDFW's rate compare to its past rates?

Our rate is returning back to historical levels for this agency. WDFW routinely had an indirect rate near 30% for several years. The low rate in FY10 includes reductions due to over-collection of indirect in previous years.

WDFW Federally-Approved Indirect Rates

FY05	FY06	FY07	FY08	FY09	FY10	FY11	FY12	Proposed FY13
29.31%	28.79%	28.89%	28.74%	25.87%	21.78%	23.32%	23.51%	28.36%

16. How does WDFW's rate compare to other agencies?

There are many appropriate ways to develop an indirect rate. Consequently, **indirect rates are not comparable across agencies.**

First, state agencies can apply indirect to different objects of expenditure. Some agencies apply it to salaries and benefits only. WDFW's indirect rate applies to most expenditures – just capital costs and fish food are excluded. Since the indirect rate is a ratio between direct and indirect costs, the rate swings wildly if you change what direct costs it applies to – even though total costs are exactly the same. In the example below, an agency indirect rate could jump 8.5% by billing indirect on direct staff costs only.

Indirect rates depend upon the costs to which it is applied

	Apply indirect to most costs	Apply indirect on salaries and benefits only
Salaries and Benefits	100,000	100,000
Goods & Services	30,000	30,000
Indirect Support Costs	37,000	37,000
TOTAL costs	167,000	167,000
Indirect Costs (A)	37,000	37,000
Direct Cost Base (B)	130,000	100,000
Indirect Rate (A/B)	28.5%	37%

Secondly, many costs can be recovered either directly or indirectly. Indirectly is often more efficient, but makes the rate higher. However, a higher indirect rate doesn't necessarily mean you are expensive. A 40% rate could cost as much as a 10% rate. How is that possible? A group that uses indirect as much as possible (to simplify billing and accounting; the right column below) will have fewer direct costs and a higher indirect rate. An organization that direct bills as much as possible (middle column below) will have fewer costs in the indirect rate model. Either way, total costs are the same, even though the indirect rates are dramatically different. In the table below, white cells show costs that are billed directly, while shaded cells are costs recovered through an indirect rate.

Same Costs, Different Indirect Rates		
Cost	Approach #1: Maximize direct billing	Approach #2: Simplify billing
Salaries & Benefits	70,000	70,000
Facility Costs	10,000	10,000
PCs and Equipment	10,000	10,000
Admin support	10,000	10,000
TOTAL	100,000	100,000
Indirect costs (shaded cells)	10,000	30,000
Direct Costs	90,000	70,000
Indirect rate	11%	43%

In WDFW's case, some of the rate increase is a result of taking some costs out of direct billing and moving them into indirect (to improve consistency and to lower costs by simplifying billing). Most of the rate increase is from a more thorough accounting of who provides indirect services that support contractual work.

17. Can some work get a lower indirect rate?

We've heard from some organizations that contract us to work on their behalf, suggesting that they don't think they really use many indirect-supported services, and therefore they should have a lower rate. We analyzed the indirect-funded services that support hatcheries as an example to see how much truth was in this claim (see Appendix A). We found that hatcheries have at least an average use of indirect support, and therefore should pay the full agency indirect rate.

Appendix A: How Much Indirect Support Does a Hatchery Really Get?

We were asked if hatcheries really should pay the full indirect rate, so convened a small group (Jeff Korth, Heather Bartlett, Lee Rolle, David Giglio) to talk through the various components of the indirect rate and evaluate whether, and to what degree, hatcheries typically use these functions. The conversation is by its nature qualitative. Below is our tabular assessment and analysis.

Admin Function/Cost	Hatchery Usage of Indirect Support
BSP – Admin Support Functions	12% of the FY13 agency proposed rate (28% total)
Contracts Staff	Yes – below average relative to the amount of earned indirect (usually big-dollar awards, with precedent)
Purchasing Staff	Yes – average to above average usage
Fiscal - Payroll	Yes – above average use from having temp/seasonal staff
Fiscal – Vendor Payments	Yes – average to above average usage
Fiscal – Accounts Receivable	Yes
Fiscal - Inventory	Yes. NOTE: some awards provide equipment or facilities for our use. These agreements will need less indirect support, but they will also pay less indirect by avoiding a direct cost. For example, if the contracting organization provides a vehicle, they avoid both the direct and the indirect costs associated with the equipment.
IT – Desktop Support, Helpdesk	Yes – above average IT needs on a per FTE basis. For many IT functions, the usage is intermittent, but hatcheries have more complex support issues because of highly variable connection types, reliance on public ISP and VPN for connectivity, low connectivity for providing remote support, and travel requirements to remote locations.
IT - Applications	Yes – the agency develops and maintains some internal applications and systems for hatcheries (Fishbooks, e.g.)
Human Resources	Yes – above average on hiring; labor, safety, training, other personnel work is lumpy (low most of the time, high other times)
BSP – Director’s Office/Agency Functions	4%
Director’s Office	These are agency-level functions. Indirect is designed to cover these costs that cannot be attributed to particular projects.
Regional Offices	
Budget	

Overhead – major costs	4%
Rent, leases, facilities	Yes – below average. NRB and regional building costs apply to a degree, as they house support functions for hatchery staff and operations. As with inventory, hatcheries often avoid provide the facility, thereby avoiding paying indirect on those costs.
DES fees	Yes
Unemployment	Yes – well above average due to seasonal/temp employees.
Attorney General Services	Highly situational – generally below average unless there is a particular issue.
IT costs (PCs, data storage)	Yes – below average due to lower PCs per staff ratio. Direct PC costs will drop out of contracts under the new indirect rate model, saving direct and indirect dollars.
Program Administration	7%
Budget and Contracts Support	Yes. The new model includes some staff who provide budget and contracts support to agreements, but had not been included in the indirect model.
Fleet and other support	Yes. The new model includes some staff who provide administrative support to agreements, but had not been included in the indirect model.
Program Leadership	Yes. The new model includes some senior managers who provide direction and support to hatcheries, but had not been included in the indirect model. Rather, they had direct billed. PUDs will pay a little less under this change (a little more indirect, but less direct).
Supervisors of contracted staff	Yes – below average usage if supervisors direct bill their time.
Recovery of unearned indirect	1%
Past indirect recovery	Yes (if the proposed rate is approved, these facilities would have underpaid in the past).

Conclusion

Hatcheries seem to use an average or above average amount of indirect support.

They may use have fewer costs associated with facilities and some other areas. However, in these areas the awards are often paying less indirect by keeping many line-item costs out of the contract. (If a PUD provides a facility, it avoids several hundred thousands of indirect.)

Additionally, hatcheries place high demands for support services in the areas of HR, payroll, and IT. The high number of seasonal and temporary staff are a major driver of these costs.

Lastly, the hatchery system receives a significant subsidy in the form of unemployment insurance. These costs are largely passed on to be paid by state funds and by earned indirect from other agreements.