DEPARTMENT OF THE TREASURY

Fiscal Service

31 CFR Part 205

RIN 1510–AA38

Rules and Procedures for Efficient Federal-State Funds Transfers

AGENCY: Financial Management Service, Fiscal Service, Treasury.

ACTION: Notice of proposed rulemaking.

SUMMARY: The Financial Management Service (FMS) proposes to revise the regulations implementing the Cash Management Improvement Act of 1990, as amended (CMIA). These regulations govern the transfer of funds between the Federal Government and States for certain Federal assistance programs. The revisions will provide greater flexibility in funding techniques; ensure that Treasury-State Agreements are unambiguous and auditable; address concerns raised by States, Federal agencies, and the General Accounting Office (GAO); delete obsolete provisions; incorporate FMS policy statements as appropriate; reflect new legislation and directives; and make the regulation clearer and, where possible, more concise.

DATES: Send your comments to reach us on or before January 10, 2001; we may not consider comments received after the above date in making our decision.

ADDRESSES: For information about filing comments electronically, see the **SUPPLEMENTARY INFORMATION** section under ''Electronic access and filing address.'' You may also mail comments to Cynthia L. Johnson, Director, Cash Management Policy and Planning Division, Financial Management Service, 401 14th Street, S.W., Room 420, Washington, D.C. 20227. You may hand deliver comments to us at that same location.

FOR FURTHER INFORMATION CONTACT: Sally Phillips, Senior Financial Program Specialist, at (202) 874–7106, or Stephen K. Kenneally, Financial Program Specialist, at (202) 874–6966, or Matthew Helfrich, Financial Program Specialist, at (202) 874–6754, or Oscar Ona, Financial Program Specialist, at (202) 874–6799, or Adam Martin, Financial Program Specialist, at (202) 874–6881, or Cynthia L. Johnson, Director, Cash Management Policy and Planning Division, at (202) 874–6657, or Ellen Neubauer, Senior Attorney, at (202) 874–6680. Individuals who use a telecommunications device for the deaf (TDD) may call the Federal Information Relay Service at 1–800–877–8339 between 8:00 a.m. and 4:00 p.m. Eastern time, Monday through Friday, excluding Federal holidays.

SUPPLEMENTARY INFORMATION:

I. Public Comment Procedures

Electronic Access and Filing Address

You may view an electronic version of this proposed rule at http://www.fms.treas.gov/policycmia and submit comments to FMS via the web site. You may also comment via e-mail to: cmia@fms.treas.gov. Please also include ''Attention: RIN—1510-AA38'' and your name, address, and phone number in your Internet message. If you do not receive a confirmation from the system that we have received your Internet message, contact us directly at (202) 874–6590.

Written Comments

Written comments on the Notice of Proposed Rulemaking (NPRM) should be specific, should be confined to issues pertinent to the proposed rule, and should explain the reason for any change you recommend. Where possible, you should reference the specific section or paragraph of the proposal you are addressing. We may not consider or include in the Administrative Record for the final rule comments which we receive after the close of the comment period.

Comments, including names, street addresses, and other information of respondents, will be available for public review at the Department of the Treasury Public Reading Room during regular business hours (8:00 a.m. to 4:00 p.m.), Monday through Friday, except Federal holidays. We will also post all comments on the CMIA policy website at http://www.fms.treas.gov/policycmia at the end of the comment period. Individual respondents may request confidentiality. If you wish to request that we consider withholding your name, street address, or other contact information (such as Internet address, FAX or phone number) from public review or from disclosure under the Freedom of Information Act, you must state this prominently at the beginning of your comment. We will honor requests for confidentiality on a case-by-case basis to the extent allowed by law. We will make available for public inspection in their entirety all submissions from organizations or businesses, and from individuals identifying themselves as representatives or officials of organizations or businesses.

Public Hearings

In addition, Treasury will hold two public hearings on the proposed rule that will provide individuals with the opportunity to publicly present their comments. The dates, times, and locations of these public hearings will be announced in a document that will be published in the **Federal Register** and made available on the CMIA Policy website at http://www.fms.treas.gov/policycmia.

II. Background

We are proposing to revise our regulations at 31 CFR Part 205 (Part 205). Part 205 implements the Cash Management Improvement Act of 1990 (CMIA), Public Law 101–453, and the Cash Management Improvement Act Amendments of 1992, Public Law 102–589, codified at 31 U.S.C. 3335, 6501, and 6503.

CMIA was enacted in order to create greater efficiency and equity in the exchange of funds between the Federal Government and the States. Prior to the enactment of CMIA, Federal agencies expressed concerns that States were drawing down Federal funds well in advance of the time those funds were needed by States. States, on the other hand, expressed concerns about having to pay out their own funds in advance of receiving funds from the Federal Government.

CMIA, which requires the heads of executive agencies to provide for the timely disbursement of Federal funds in accordance with regulations prescribed by the Secretary of the Treasury, has three major provisions designed to address these issues:

- States and Federal agencies must minimize the time between the transfer of funds from the U.S. Treasury and the clearance of funds out of the accounts of a State.
- The Secretary of the Treasury shall enter into a Treasury-State Agreement with each State which specifies the funds transfer procedures for Federal assistance programs.
- In general, States and the Federal Government are respectively entitled to interest when the other fails to make funds transfers in a timely fashion. States owe the Federal Government interest for the time Federal funds are in State accounts before they are spent for Federal assistance program purposes. A Federal agency owes a State interest if the State disburses its own funds with obligational authority to support the Federal portion of a program before receiving Federal funds.

We issued Part 205 in 1992. The Final Rule was published on September 24, 1992 (57 FR 44272). The foundation of

the regulation was the use of recognized, sound cash management principles in order to increase certainty in the timeliness of payments between Federal agencies and States. Since 1992, we have issued a number of CMIA Policy Statements (Policy Statements) that address various issues relevant to Part 205.

One of the purposes of the proposed rulemaking is to update the current regulation by deleting obsolete provisions and incorporating FMS Policy Statements. Another purpose is to address various concerns that States, Federal agencies, and the General Accounting Office [1] have raised since the issuance of Part 205. Specifically, the proposed regulation:

(1) Provides greater flexibility in funding techniques;

(2) Ensures that Treasury-State Agreements are unambiguous and auditable;

(3) Reflects new legislation and directives, including the Single Audit Act Amendments of 1996, 31 U.S.C. Chapter 75; and Executive Order 12866 of September 30, 1993, Regulatory Planning and Review; and,

(4) Makes the regulation clearer and, where possible, more concise.

FMS provided an earlier draft of this proposed rule to the National Association of State Auditors, Comptrollers and Treasurers, the National Governors' Association, the National Conference of State Legislatures, the Council of State Governments, and the National League of Cities and solicited comments from their membership. We also provided the draft proposed rule to the state of Colorado. We received several comments which have been considered in the formulation of this rule.

III. Discussion of Proposed Rule

General. We are proposing to reorganize subpart A of Part 205 by presenting general information on Treasury-State Agreements first, followed by specific information related to the various sections of a Treasury-State Agreement. The proposal consolidates requirements related to specific programs into one section. In addition, the proposed reorganization puts State oversight and compliance requirements in one section, and Federal agency requirements in another. Proposed subpart B combines the existing two subsections on the consequences of Federal and State noncompliance since the result of noncompliance by either party is the same for the noncomplying party. Subpart C continues to be reserved.

[1] See Financial Management: ''Implementation of the Cash Management Improvement Act'' (Letter Report, 01/08/96, GAO/AIMD–96–4).

Although the format is different due to recently enacted plain language requirements, the proposed rule is consistent with the existing rule except where specifically noted. Incorporating existing Policy Statements into the regulation has also altered the rule's appearance. The proposed changes have been made based on input received from key program stakeholders: States and Federal program agencies.

Disallowances. Section 205.2 of the proposed rule defines disallowances as costs incurred by a State which the Federal program agency determines to be costs which should not be charged to the Federal Government either because the funds were used for other than Federal assistance program purposes or the amount of the funds used for Federal assistance program purposes was improper. Section 205.15 of the proposed rule adds a provision expressly recognizing that disallowances are subject to the CMIA's interest provisions.

Generally, disallowances occur when a Federal agency determines that a request for funds submitted by a State is invalid because the funds are not used for legitimate Federal assistance program purposes or the amount of funds used or requested for Federal assistance purposes was improper. A Federal agency may disallow a funds transfer prior to it being made to a State or after it is made to a State. In some cases, the statutes governing a specific program address disallowances and assess interest penalties. The CMIA allows Treasury to consider such statutory provisions when determining whether the CMIA interest provisions apply to particular disallowances.

This rule does not change the way an expenditure is determined to be a disallowance. Whether or not funds expended by a State should be properly charged to the Federal government is a determination to be made by the Federal program agency responsible for the Federal assistance program under which the expenditure arose. As in the past, this determination will be made in accordance with the statutes, regulations, and policies applicable to that program.

We are specifically seeking comment from States, Federal agencies, and the public on the implementation of the disallowance provisions.

Section-by-Section Analysis

Section 205.1 What Federal Assistance Programs Are Covered by This Part?

Proposed § 205.1 replaces current § 205.1, *Purpose*, and current § 205.2, *Scope*. Proposed § 205.1 states that the rule applies to all States and Federal program agencies (except the Tennessee Valley Authority) and covers programs listed in the Catalogue of Domestic Federal Assistance.

Section 205.2 What Definitions Apply to This Part?

Proposed § 205.2 replaces current § 205.3, titled *Definitions*. Based on input from Federal agencies and States during several years of CMIA implementation, we're proposing certain deletions, additions, and modifications to the definitions. Three definitions are deleted: equivalent rate, issue checks, and program. Twenty-three definitions are added: administrative costs, business day, Catalog of Federal Domestic Assistance, compensating balance, default procedures, direct cost, disallowances, dollar-weighted average day of clearance, drawdown as a verb, estimate, Federal assistance program, Financial Management Service, grant, indirect cost, indirect cost rate, maintenance-of-effort, rebate, refund transaction, reverse flow program, revolving loan fund, Treasury-State Agreement, vendor payment, and we and us. Additionally, the table describing the applicable dollar thresholds for major Federal assistance programs found in Appendix A of current subpart A is moved to proposed § 205.5, *What are the thresholds for major Federal assistance programs?* since the proposed rule addresses program eligibility in that section.

Subpart A: Rules Applicable to Federal Assistance Programs Included in a Treasury-State Agreement

Section 205.3 What Federal Assistance Programs Are Subject to Subpart A?

Proposed § 205.3 replaces portions of current § 205.4, *Scope of subpart*. This section provides criteria by which States and Federal agencies determine which programs are covered by this Part in general, and by subpart A in particular.

Proposed § 205.3 clarifies that, at the discretion of the State, the number of programs included in a Treasury-State Agreement can be increased by lowering the funding thresholds. Lowering the funding threshold as a means of expanding permissible program coverage avoids disputes over individual programs. Federal agencies were concerned that States would try to add individual programs under which the Federal Government would likely incur interest liabilities to the States. States, on the other hand, were concerned that the Federal Government would oppose adding specific programs

with likely Federal interest liabilities and instead move to cover programs under which the States would likely incur interest obligations.

Since they are no longer applicable, the subsections in current Part 205 on initial program coverage and the grace period for colleges and universities are deleted in the proposed rule.

These sections applied only to the first year of CMIA implementation.

We are seeking comment from Federal program agencies and States on reducing the administrative burden associated with the requirements of subpart A. In particular, we seek input on methods granting relief, consistent with the CMIA, to States and Federal program agencies that practice good cash management.

Section 205.4 Are There Any Circumstances Where a Federal Assistance Program That Meets the Criteria of 205.3 Would Not Be Subject to Subpart A?

Proposed § 205.4 replaces portions of existing § 205.4, *Scope of Subpart.* Proposed § 205.4 outlines a few exceptions to the regulation regarding the applicability of subpart A to some Federal assistance programs. Although the section heading is new, these exemptions are not new and exist in the current rule or are included in Policy Statements. Some examples of exempted programs are those that have been discontinued and whose remaining funding is below the major program threshold and those administered through several State agencies provided certain other requirements are met.

Proposed § 205.4 includes a provision integrating Policy Statement 8 (''Materiality Exemptions,'' April 19, 1993). Proposed § 205.4 describes exemptions for components of certain Federal programs that are spread over several agencies within a State. If a State agency's portion of the funding does not exceed 5% of the State's major Federal assistance threshold or 10% of total program expenditures, the regulation allows us and a State to exclude that portion of the funding from subpart A of Part 205. For example, a State Human Services agency and a State Agriculture Agency may share responsibility for a Federally funded nutrition program. If the share of funding received by the State Agriculture Agency falls within the limits given above, funds received are not subject to subpart A of Part 205. However, if interest liability is found in the State Human Services agency's portion of the program that is subject to this Part, the interest liabilities should be pro-rated to reflect interest on 100% of the program's funding.

Proposed § 205.4 also includes a provision integrating Policy Statement 17 (''Exclusion of Major Federal Assistance Programs Based on Funding Changes'', June 21, 1995), which describes exemptions for discontinued programs. Specifically, we and a State may agree to exempt a program from being subject to Part 205 if the program has been discontinued and the remaining funding does not exceed the existing major program threshold. We may also agree with a State to exempt from subpart A of Part 205 multi-year programs that have remaining funds totaling less than that of a State's threshold. For example, assume a five-year program has spent all but $100,000 of its authorized funds in its first four years. If the major program threshold for that State is $900,000, we and a State can agree to exempt the program from subpart A of Part 205 program for its one remaining year.

Section 205.5 What Are the Thresholds for Major Federal Assistance Programs?

In the current rule, § 205.5 is reserved. In the proposed rule, this section is used to state the threshold determination levels and incorporate Appendix A from the current rule.

A small number of Federal programs are responsible for the majority of interest exchanged each year. In general, these are the largest Federal assistance programs, based on funding levels. The proposed rule increases the existing thresholds, thereby reducing the number of programs covered.

As with the current rule, the proposed rule requires States to determine the major program thresholds based on a percentage of the total expenditure of Federal assistance by a State. Different percentages are applied based on the amount of Federal assistance received by a State. The proposed rule doubles the percentages used in the existing rule. For example, States that receive $100 million or less would apply a 6.00 percent standard under the proposed rule instead of the 3.00 percent standard currently in effect. States that receive between $100 million and $10 billion would apply a 0.60 percent standard instead of 0.30 percent standard. States receiving in excess of $10 billion in Federal assistance must apply a 0.30 percent standard instead of the 0.15 percent standard. However, States in this largest category are subject to a default threshold level of $60 million or greater. This is to ensure that the threshold is at least as great as for those States in the middle category. Under the proposed rule, States do not have the option of selecting a fixed dollar amount instead of the percentage. This reduces the number of applicable threshold levels from ten to three.

The higher thresholds allow States, Federal program agencies, and FMS to focus their resources on large dollar programs and eliminate the administrative burden of tracking interest liabilities for numerous, but relatively small, Federal assistance programs. A review of the potential effect of approximately doubling the major program threshold indicates that the eliminated programs represent a very small percentage of the program funds that would remain subject to this Part. This is because the eliminated programs represent the smallest programs, measured by dollar amount, covered by CMIA.

To ensure that adequate program coverage is maintained, the proposed regulation requires a State to compare its coverage under the new thresholds with program coverage under the existing thresholds determined by the Single Audit Act. Consider, for example, a State that has a threshold of $10 million under the existing regulation, using the current 0.3 percent multiplier, and would have its threshold doubled to $20 million under the proposed regulation using the 0.6 percent multiplier. That State must sum the total dollar value of the additional programs that would be exempted under the proposed rule. If that figure exceeds 10 percent of the total dollar value of the programs covered using the lower threshold amount, then the threshold must be lowered until 90 percent coverage of the total program dollars is maintained.

Assume, for purposes of our example that, under the existing regulations the State's $10 million dollar threshold would cover 24 programs that represent a total value of $600 million. Under the proposed regulation, the threshold rises to $20 million, covering 15 programs that total $530 million. To determine if 90% coverage is maintained, the State must divide the reduction in total program coverage by the program coverage value under the existing rule or ($600 million − $530 million)/$600 million=11.6 percent. In this case, program coverage would be reduced by more than 10% and the threshold level would be adjusted downward until that level of coverage is reached. The 10% reduction in program coverage is not a target, but an outer limit. A State that doubles its threshold which eliminates less than 10% of its total program dollar coverage is NOT allowed to automatically increase its threshold to reach the 10% level.

As noted in § 205.3, States that wish to retain or expand current CMIA program coverage would be allowed to continue to negotiate Treasury-State Agreements containing lower program thresholds.

To determine if a program meets the threshold for a ''major'' program, refer to Table A in proposed § 205.5. For example, assume a State receives $3 billion in Federal assistance for all programs. To determine which programs are major Federal assistance programs, look at the corresponding information in Column B. Column B indicates that any program with expenditures exceeding 0.60 percent of the total Federal assistance expenditures would be considered a major Federal assistance program. Under the proposed rule, the State calculates the threshold by multiplying $3 billion by 0.60 percent, totaling $18 million.

On May 5, 1999, the current regulation was revised with updated major program threshold criteria derived from the Single Audit Act Amendments of 1996, 64 FR 24242. We are now proposing to move the amended table describing these thresholds to proposed § 205.5 from the definitions section of the current rule. The Single Audit Act Amendments of 1996 identify programs subject to audit based on a combination of objective funding figures and a subjective ''risk'' analysis of each program. The ''risk based'' criteria do not apply to this Part. The only criterion for designation as a major program subject to this Part is funding level.

Section 205.6 What Is a Treasury-State Agreement?

Proposed § 205.6 includes provisions found in current § 205.9, *Treasury-State Agreements.* Provisions from current § 205.6, *Funding Techniques* are moved to proposed § 205.12. A Treasury-State Agreement is a document negotiated by FMS and the States that identifies the covered programs, funding techniques, and interest calculation methods used for programs subject to subpart A.

We are proposing a major change in the Treasury-State Agreement negotiation process. Currently, the majority of Treasury-State Agreements have a one-year term and thus must be renegotiated annually. We do not believe that it is necessary or productive to renegotiate each agreement every year, particularly since agreements are amended as necessary to reflect changes in programs, funding techniques, and clearance patterns. Therefore, we are proposing to make Treasury-State Agreements effective until terminated. States and the Federal Government retain the right to terminate a Treasury-State Agreement with 30 days written notice.

Section 205.7 Can a Treasury-State Agreement Be Amended?

Proposed § 205.7 is a new section that contains details on the amendment process currently set forth in Policy Statement 10 (''Amendment Policy and Process,'' May 11, 1994). In general, proposed § 205.7 indicates how, when, and for what reason States can amend Treasury-State Agreements. A State may amend a Treasury-State Agreement for such reasons as: adding or deleting programs, changing funding techniques, and changing clearance patterns.

Section 205.8 What if There Is No Treasury-State Agreement in Effect?

This section addresses the default process that is currently part of existing § 205.9 *Treasury-State Agreements.* It describes the situation when there is no Treasury-State Agreement in effect. In these circumstances, we will prescribe default procedures to implement subpart A. We will identify the major programs to be subject to subpart A as well as the funding techniques to be used by the State.

Section 205.9 What Is Included in a Treasury-State Agreement?

Proposed § 205.9 is similar to current § 205.9 in that it describes the components that must be included in a Treasury-State Agreement. Proposed § 205.9 also prescribes a uniform format for Treasury-State Agreements. Although we have made an effort in the past to standardize the format of the first-year agreements, most agreements still have differences in format. These differing formats add to the time needed to review the agreements and make it difficult to examine and compare them. Proposed § 205.9 is designed to correct this problem, but it is not intended to change the substantive provisions of the agreements. We'll provide the new format to the designated State and Federal agency CMIA contacts. The format will consist of terms and conditions common to all States, followed by addenda specific to any one State.

Section 205.10 How Do You Document Funding Techniques?

Proposed § 205.10 replaces current § 205.7, *Requesting and transferring funds.* Proposed § 205.10 clarifies the information on funding techniques that must be included in a Treasury-State Agreement. Concise descriptions of each funding technique must include details such as ''what is a timely request for funds?'' and ''what procedures are used to reconcile estimates with actual cash needs?'

It is important to include these details in the negotiated Treasury-State Agreement because we aren't requiring any particular funding techniques. Therefore, it will benefit all parties to have the terms of the agreed upon funding techniques clearly described.

Section 205.11 What Requirements Apply to Funding Techniques?

Proposed § 205.11 contains basic requirements a State and a Federal agency have to meet to achieve an efficient level of funds transfers. Proposed § 205.11 restates much of current § 205.11. In addition, proposed § 205.11 mandates electronic funds transfer for Federal funds transfers to States, pursuant to the Debt Collection Improvement Act of 1996 and its implementing regulation, 31 CFR Part 208. 63 FR 51490. The definition of electronic funds transfer found in proposed § 205.2 has been expanded beyond wire transfers and Automated Clearing House payments to include any payment made electronically.

In response to the questions received from States on the treatment of compensating balances under CMIA, proposed § 205.11(c) provides that a State must not draw down funds from its account in the Unemployment Trust Fund or from a Federal account in the Unemployment Trust Fund in advance of actual immediate cash needs for the express purpose of maintaining a compensating balance. Compensating balances are deposits held in bank accounts to offset the costs of bank services.

CMIA requires States and Federal agencies to minimize the time between the drawdown and the subsequent expenditure of Federal funds for Federal assistance program purposes. Thus, a State may only draw down Federal funds in accordance with the timing and amounts dictated by the agreed upon funding technique. The amount drawn down must equal the amount issued or the amount expected to clear. Drawdowns may not include an extra amount, or occur earlier, to create a balance for the purpose of compensating a bank. A State's interest liability on funds withdrawn from a State account in the Unemployment Trust Fund is based on actual interest earned. The proposed rule clarifies that actual interest earned does not include non-cash bank earnings.

Section 205.12 What Funding Techniques May Be Used?

Proposed § 205.12 contains much of current § 205.6, *Funding techniques.* However, proposed § 205.12 states in clear language that the funding techniques listed in the section are not the only methods allowed. The General Accounting Office report, ''Financial Management: Implementation of the Cash Management Improvement Act,'' January 1996, noted that States found the restrictions on the use of reimbursable funding burdensome. In response, FMS is giving States more flexibility in choosing funding techniques. However, we believe that there is value in providing definitions of some funding techniques. States and Federal agencies may benefit from having a standard definition when negotiating a Treasury-State Agreement. The definitions in proposed § 205.12 may be adopted, modified, or excluded from a Treasury-State Agreement at the discretion of the parties negotiating the agreement.

The proposal allows States and Federal program agencies to negotiate the use of a technique that meets their needs, including reimbursable funding, which is currently prohibited. Reimbursable funding is a funds transfer method where, after a State pays out its own funds for the Federal portion of a program, the State then requests and receives reimbursement for the Federal funds paid out by the State. The proposal would eliminate the current prohibition on reimbursable funding.

We're proposing this change because some States have used reimbursable funding to fund certain administrative and overhead costs through cost allocation or other after-the-fact distribution methods. We expect to limit the use of reimbursable funding to those limited circumstances where there aren't any other acceptable funding techniques.

Section 205.13 How Do You Determine When State or Federal Interest Liability Accrues?

Proposed § 205.13 is a new separate section that clarifies that State or Federal interest liability may accrue when funding techniques agreed to in the Treasury-State Agreement are applied. Proposed § 205.13 contains a provision included in existing § 205.10 that allows a State and FMS to agree not to assess interest liability for indirect costs or indirect allocated costs. These costs would be based on an indirect cost rate and the arrangement must be included in the Treasury-State Agreement.

Section 205.14 When Does Federal Interest Liability Accrue?

Proposed § 205.14 replaces current § 205.11 governing Federal interest liabilities. In general, the Federal government incurs an interest liability if the State pays out its own funds for Federal assistance program purposes with valid obligational authority. Obligational authority is defined as ''the existence of a definite commitment on the part of the Federal government to provide appropriated funds to a State to carry out specified programs, whether the commitment is executed before or after a State pays out funds for Federal assistance program purposes.'' Thus, obligational authority exists if the Federal government is authorized to make payments to a State and appropriates funds to make those payments. If a State pays out funds for Federal assistance program purposes before Congress has appropriated funds, and Congress subsequently appropriates funds to cover the period for which the State paid out the funds, obligational authority exists and the Federal Government incurs an interest liability to the State.

Some Federal agencies have questioned whether obligational authority exists if a State's expenditure of funds is subject to agency approval or authorization, and the State pays out funds prior to obtaining the agency's approval or authorization. We invite agencies and States to comment on the nature and operation of any agency approval requirements that currently are in place, including whether the agency's approval or authorization requirement is imposed pursuant to a Federal statute, a Federal regulation, or an agreement between the Federal agency and the State. We also request comment on whether we should amend the definition of ''obligational authority'' in the regulation to address this issue more specifically.

Proposed § 205.14(a)(3) clarifies that a Federal agency does not accrue retroactive interest liability if a State expends funds for a discretionary grant project prior to receiving approval from the Federal agency. A discretionary grant is a project for which a Federal program agency is authorized by law to exercise judgment in awarding a grant and in selecting a grantee, generally through a competitive process. CMIA interest liability on discretionary grants cannot begin to accrue until the Federal program agency approves the project. This position is consistent with the existing regulation.

Proposed § 205.14(a)(5) includes a provision that allows FMS to deny Federal interest liability if a State fails to follow the agreed upon procedures outlined in the Treasury-State Agreement. The intent of this regulation, efficient cash management, is best accomplished when all parties comply with the Treasury-State Agreement.

Section 205.15 When Does State Interest Liability Accrue?

Proposed § 205.15 replaces current § 205.12 describing the circumstances under which State interest liability accrues.

Proposed § 205.15(b) provides that States will incur an interest liability on disallowances. The CMIA states the following: ''The Secretary shall issue regulations that shall require a State, when not inconsistent with Federal assistance program purposes, to pay interest to the United States on funds from the time funds are deposited by the United States to the State's account until the time that funds are paid out by the State in order to redeem checks or warrants or make payments by other means for program purposes.'' Disallowed funds are funds that have been paid out for other than Federal assistance program purposes and, therefore, are not properly chargeable to the Federal government. Under CMIA, a State must pay interest to the United States on such funds.

In general, if a Federal program agency disallows a State expenditure, a State will owe interest from the day on which the Federal funds associated with the disallowed expenditure were credited to the State's account to the day the funds are credited back to the Federal government. In many instances, however, State expenditures are disallowed by a Federal program agency in CMIA reporting years subsequent to the CMIA reporting year in which the State originally made the expenditure. In such instances, either the State or the Federal government may previously have paid CMIA interest on the funds associated with the disallowed expenditure. The State's CMIA interest calculation resulting from the disallowance shall be adjusted to reflect any prior CMIA interest payments.

For example, a State may have paid interest to the Federal government in the reporting year in which the State made the expenditure because the State drew down Federal funds early. In that case, the State's interest liability resulting from the disallowance should be reduced by the amount of interest it had already paid in the earlier reporting year (i.e., interest accruing from the day the State drew down the funds until the State paid out the funds). Alternatively,

the Federal government may have paid interest to a State in an earlier reporting year because the State advanced the funds associated with the disallowed expenditure. Because the State did not pay out the funds for Federal assistance program purposes, the State was not entitled to the interest that the Federal government paid for that period. Accordingly, the State must reimburse the Federal government for that interest, and the State's liability resulting from the disallowance must be increased accordingly.

FMS is specifically seeking comment on the implementation of this provision.

Proposed § 205.15(c)(2)changes the current provision allowing States and FMS to agree on a refund transaction exemption threshold of $10,000. The proposed rule lets FMS and a State mutually agree on either a $50,000 threshold or no refund transaction threshold. The purpose of the threshold is to give States relief from tracking large volumes of small dollar refunds. The General Accounting Office report noted that some States believe excessive effort is required to monitor and calculate interest on refunds. Some States adopted labor-intensive procedures to separate refund transactions above the threshold from those below it, and to calculate interest on each refund transaction rather than an aggregate refund activity.

Section 205.16 What Special Rules Apply to Federal Assistance Programs and Projects Funded by the Highway Trust Fund?

Proposed § 205.16 contains provisions currently included in § 205.11, *Federal interest liabilities.* Some States have asked FMS to clarify the Federal interest provisions for programs and projects funded from the Federal Highway Trust Fund. If a State pays out its own funds in the absence of a project agreement, the Federal Government will not incur an interest liability, even if obligational authority is established subsequently to permit payment for the State's expenditure. This is the current policy, and it remains unchanged in the proposed rule. Where a project agreement exists, States must request funds at least weekly for current project costs. The Federal Government will accrue an interest liability on current project costs for which there is valid obligational authority, for a maximum of one week's time. The Federal Government will not accrue an interest liability on project costs accrued prior to the week the State request funds.

Section 205.17 Are Funds Transfers Delayed by Automated Payment Systems Restrictions Based on the Size and Timing of the Drawdown Request Subject to This Part?

Proposed § 205.17 clarifies the role Part 205 plays when funds transfers are delayed by a Federal program agency. Part 205 applies to funds transfers that are deferred by a Federal program agency based solely on the size and timing of the drawdown request. This is in response to State concerns that payment systems such as the Automated Standard Application for Payment (ASAP) and the Payment Management System (PMS) may allow Federal program agencies to automatically reject drawdown requests that fall outside a predetermined set of parameters.

Section 205.18 Are Federal Program Agency Grants for Administrative Costs Subject to This Part?

Proposed § 205.18 clarifies the treatment of grants made to States to compensate for indirect administrative costs. This subject is addressed in current § 205.10, *Funding of indirect costs and administrative costs.* We are proposing these changes in response to concerns that tracking these costs is not an efficient use of resources. These two provisions make clear that Federal agency grants that are 100% dedicated to compensate for indirect and/or other administrative costs are subject to subpart A. However, as for grants that contain funds dedicated to program costs and administrative costs, the portion of the grant dedicated to indirect administrative costs is not subject to Part 205.

Section 205.19 How Is Interest Calculated?

Proposed § 205.19 incorporates the provisions of current § 205.13, *Interest calculation.* Proposed § 205.19 lists the requirements that States must comply with to calculate and support interest liability claims. States must ensure that the interest calculations are auditable and retain a record of the calculations. This section also describes the method used to calculate the interest rate applied to CMIA liabilities. We will provide that interest rate to each State.

Section 205.20 What Is a Clearance Pattern?

Proposed § 205.20 contains information found in current § 205.8, as well as more detailed information regarding the requirements of developing and maintaining proper clearance patterns. These requirements are intended to ensure that all clearance patterns meet an adequate level of accuracy and detail. In general, a clearance pattern must accurately represent the flow of Federal funds under the Federal assistance programs. These clearance patterns must be based on at least three consecutive months of disbursement data, and valid statistical sampling must be applied.

Several States have requested a clearer statement of the standards to be used in developing clearance patterns. Therefore, the proposed rule specifies:

(1) The information that must be included in a Treasury-State Agreement, consistent with proposed § 205.9;

(2) The amount of data to be used to develop a clearance pattern;

(3) The standards of statistical accuracy to be applied if checks are sampled to develop a clearance pattern; and

(4) the range of days which a clearance pattern must cover.

Some States have questioned why we require that a clearance pattern be carried out until 99 percent of the dollars in a disbursement clear or are paid out for Federal assistance program purposes. The States' concern was noted in the General Accounting Office report, ''Financial Management: Implementation of the Cash Management Improvement Act,'' January 1996. The 99 percent standard, currently documented in FMS Policy Statement 11 (''Clearance Patterns,'' May 20, 1994), is incorporated in the proposed rule. The 99 percent standard was adopted because the 95 percent standard did not accurately represent the flow of funds, leaving a substantial amount of funding undocumented.

When CMIA was initially implemented, we required that a clearance pattern be carried out until 95% of the dollars cleared. At that time, only a limited amount of clearance data were available. When additional clearance data became available, we learned that some States do not have expiration dates for checks; thus, checks could remain outstanding for years. The 95 percent standard allowed States to draw down 5 percent of Federal funds before the dollars cleared. Further, the 95 percent clearance standard allowed the dollar-weighted average day of clearance to be one day earlier than with the 99 percent standard.

A clearance pattern based on either the old 95 percent standard or the current 99 percent standard may extend over a significant period of time. Some States are concerned about making numerous small drawdowns, as noted in the GAO report. There are many ways to avoid this, such as the use of average clearance. A State also may use estimated clearance for a period of time

specified in its Treasury-State Agreement. A State may use estimated clearance for the first two weeks of the clearance pattern, then make one additional drawdown on the average day of clearance of the remaining funds.

Section 205.21 When May Clearance Patterns Be Used?

Proposed § 205.21 through § 205.23 address specific issues regarding clearance patterns, found in current § 205.8, *Clearance patterns.* A State may use clearance patterns to estimate when funds are paid out, given a known dollar amount and a known date of disbursement. When the dollar amount and/or the timing of disbursements are not known, we may agree with a State on other procedures to use to estimate when funds are paid out. Clearance patterns may be used to determine the flow of funds for individual Federal assistance programs, accounts at financial institutions, groups of Federal assistance programs, and other types of payments. The methods used to create and maintain clearance patterns must be contained in the Treasury-State Agreement.

Section 205.22 How Are Accurate Clearance Patterns Maintained?

If a State has knowledge that a clearance pattern is no longer accurate, it must notify us. The State must develop a new and accurate clearance pattern, certify it, and submit it to us. Clearance patterns must be re-certified by the authorized State official every five years.

Section 205.23 What Requirements Apply to Estimates?

A major change that we are proposing to the current rule is the introduction of standards for developing, documenting, and maintaining estimates, other than clearance patterns, used to determine the amount to request and the timing of the transfer of funds. Many States have negotiated unique funding techniques that are not based on the actual amount of funds in a disbursement, but rely on some method of estimating the State's cash requirements. Often these funding techniques are difficult to audit because they are not documented in sufficient detail. The proposed standards are designed to ensure that, when such estimates are used, a Treasury-State Agreement clearly documents how to calculate the amount to request, the timing of the transfer of funds, and the method for reconciling estimates and actual payments for Federal assistance program purposes.

Estimates are used for predicting program volume for non-payment variables. For example, under a Child Care program, a State would need to estimate the increase or decrease of children needing care. This could be based on population growth or a change in the unemployment rate, or other factors. These estimates will affect the amount of funds a State draws down. The new language requires that States document and justify their estimates.

Section 205.24 How Are Accurate Estimates Maintained?

The proposed rule requires that States notify us immediately when they possess actual or constructive knowledge that the estimates in use are not accurate. This is similar to the requirement that States inform us of changes in clearance patterns.

Section 205.25 How Does This Part Apply to Certain Federal Assistance Programs or Funds?

Proposed § 205.25 contains information on how Part 205 affects several different programs.

Unemployment Trust Fund (UTF)

Proposed § 205.25 describes the treatment of the UTF under Part 205. A state's interest liability on funds withdrawn from its UTF account do not accrue at the designated CMIA rate. Instead, the interest is calculated at the actual interest earned on those funds less the related banking costs. To maintain an accurate interest calculation, if funds that are withdrawn from a State UTF account are commingled with other monies, the UTF funds must be allocated a proportional share of the related interest earnings and banking costs.

Interest earned on funds withdrawn by a State from a Federal UTF account, with the exception of the Federal Unemployment Account, will accrue under the rules of this Part, specifically, § 205.19.

Supplemental Security Income

Proposed § 205.25 sets forth the treatment of Supplemental Security Income transactions under CMIA. This subsection describes the effect of this Part on Supplemental Security Income administrative fees and supplemental State payments by integrating Policy Statement 4 (''Interest Calculations for the Supplemental Security Income Program,'' February 22, 1993,) and Policy Statement 14 (''Supplemental Security Income Program Fees,'' December 21, 1994) into the regulation.

For the most part, Part 205 applies to programs in which money flows from the Federal Government to the State. SSI is unique under CMIA in that it is a program in which money flows from the State to the Federal Government. Congress especially addressed this ''reverse flow'' in 31 U.S.C. 6503(g), which provides:

> If the Federal Government makes a payment to a recipient under a Federal program, and a portion of that payment is an amount which the Federal Government is paying to such recipient on behalf of a State, such amounts will be considered a transfer of funds between the Federal Government and the State for purposes of this section.

Interest must be calculated on the difference between a State's monthly SSI payment, which is an estimate, and the State's actual liability. This is consistent with other requirements to calculate interest on quarterly shortfalls or reporting period adjustments.

Interest liabilities shall not accrue to the Federal Government or States on refunds of State funds because States are credited with the refunds in advance, before the Social Security Administration even collects the funds. Rather than being liable for interest, the Federal Government bears the cost of crediting States with refunds early.

This provision makes it clear that the only SSI funds that are subject to CMIA are payments to recipients. Since the new administrative fees are not funds to be delivered to recipients, they are not considered a transfer of funds and, therefore, are not governed by CMIA. Interest on late fees is calculated in accordance with the Social Security Administration's (SSA) debt collection procedures.

Under the SSI program, States may supplement the Federal SSI benefit. States where the Federal SSI benefit would be less than beneficiaries received under State programs prior to SSI must supplement the Federal SSI benefit. All but a few States and jurisdictions provide supplementation. States may administer their supplementary payments themselves or may contract with the SSA for Federal administration. The SSA administers the State supplementation of SSI benefits in 27 States and the District of Columbia. Interest on late State supplementation is calculated in accordance with the provisions of Part 205.

Child Support Enforcement Program transactions

Proposed § 205.25(d) incorporates Policy Statement 6 (''Funds Collected by States Under the Child Support Enforcement Program,'' February 26, 1993), which describes the treatment for CMIA purposes of certain funds received under the Child Support Enforcement Program.

The interest provisions of CMIA do not come into play with respect to child support collections by States. Federal law provides that the Federal government will reimburse States for a portion of a State's expenditures in administering a State child support enforcement program, conditioned on the State's complying with Federal assistance program requirements. When a State collects child support, the Federal funding scheme allows the State to retain certain collections for a period of time rather than immediately distributing them to custodial parents. CMIA interest does not accrue on such undistributed funds because they are considered still paid out for Federal assistance program purposes. Rather, interest earned on undistributed funds is treated as program income under program regulations found at 45 CFR 304.50(b) and, in accordance with those regulations, must be deducted from a State's claim to the Federal government for reimbursement. Additionally, late payment fees collected by States from absent parents, as permitted by the Federal funding scheme, are not subject to interest liabilities under CMIA. These fees are State funds and are not considered Federal funds for CMIA purposes. In accordance with program regulations found at 45 CFR 302.75(b)(6), such fees must be treated as program income and must be deducted from a State's claim to the Federal government for reimbursement.

Block Grant Programs

Proposed § 205.25(e) provides clarification on Part 205's effect on certain block grant programs. This section incorporates information included in Policy Statement 7 (''Interest Provisions for Block Grants Where States Voluntarily Supplement Federal Funding,'' March 31, 1993) related to Social Services Block Grants (SSBG) and Policy Statement 19 (''Inclusion of the New Temporary Assistance to Needy Families and the New Matching and Mandatory Child Care Funds Programs Under CMIA,'' June 1, 1999). Proposed § 205.25(e) is meant to implement a policy that favors neither States nor Federal agencies participating in block grant programs.

States that supplement SSBG funding with their own funds are not allowed to draw down all Federal funds first, then use State funds. A State must draw down Federal funds in proportion to the State's participation in the block grant program.

Policy Statement 7 addresses two questions: (1) If a State voluntarily supplements the SSBG program, can the Federal program agency limit the drawdowns to be made quarterly, forcing States to supplement funds, or will this limitation result in an interest liability for the agency? (2) Can a State draw and spend all Federal funds for allowable expenses first, then spend State funds?

Federal law requires all definite appropriations to be apportioned to prevent obligation at a rate that would result in a deficiency or necessitate a supplemental appropriation. For example, if a program is expected to use funds at a constant rate and receives a quarterly Federal payment, the drawdown should be ¼ of the total amount. Given the nature of the SSBG program, it is expected that the Office of Management and Budget will continue to apportion funds quarterly. Policy Statement 7 clarifies that States are entitled to interest if they must advance their own funds due to funding breakdowns caused by apportionments.

With SSBG programs, the State is under no obligation to match or appropriate funding. However, if a State elects to appropriate funding (as opposed to temporarily fronting State funds pending reimbursement at the start of the next fiscal quarter), the State may not arbitrarily assign its earliest costs to the Federal Government and claim interest.

If a State elects to appropriate funding for the SSBG program, which does not require matching or State appropriations, funds should be allocated in a manner that benefits neither the Federal Government nor the State with respect to cash flow. Consequently, Federal funds and State funds should be combined and allocated proportionately with no interest ramifications until the combined quarterly allocation is exceeded. For example, if the total Federal allotment to a State for a given program is $16 million ($4M per quarter) and the State voluntarily appropriates $8 million ($2M per quarter), interest liabilities could occur once $6 million is paid out in any given quarter. Under this scenario, neither party ''wins'' regarding cash flow. Therefore, a State cannot draw and exhaust Federal funds first because voluntary funds which the State appropriates must be made commensurately with each Federal drawdown. In addition, States should indicate in their Treasury-State Agreement if State appropriations will currently supplement, or have historically supplemented, Federal block grants or programs which do not require a State match. If States claim interest liabilities have been incurred, Annual Reports should provide the amount of the State appropriation and State apportionment procedure.

Policy Statement 19 refers to Temporary Assistance to Needy Families (TANF) and Mandatory and Matching Child Care Funds Programs that require a State maintenance-of-effort for funding. This Policy Statement reaffirms Policy Statement 7 that Federal funds must not be drawn down in advance of, or out of proportion with, State funds used in these programs.

Women, Infants, and Children Program

Proposed § 205.25(f) is added to the regulation to clarify that interest earned on rebates from the Women, Infants, and Children Program (WIC) is not subject to Part 205 if the funds are used for Federal assistance program purposes. As noted in Policy Statement 18 (''Special Supplemental Food Program for WIC Rebates,'' September 13, 1995), this subsection recognizes the November 2, 1994 amendment to the Child Nutrition Act of 1966. That amendment declared that States will not incur any interest liability to the Federal Government on rebate funds for infant formula and other foods provided all interest earned by the State on funds is used for Federal assistance program purposes.

Revolving Loan Funds

Proposed § 205.25(g) incorporates Policy Statement 15 (''Community Development Block Grant Revolving Loan Funds,'' March 13, 1995), which describes the effect of Part 205 on revolving loan funds. Although Policy Statement 15 addresses a question on one specific program, proposed § 205.25(g) applies to all revolving loan fund programs. If a Federal agency program authorizes a revolving loan fund and specifically designates that income earned from that fund be used for Federal assistance program purposes, then the interest earned is not subject to this Part if it is used for Federal assistance program purposes. However, transfers of funds to the revolving loan fund remain subject to Part 205.

Section 205.26 What Are the Requirements for Creating Annual Reports?

Proposed § 205.26 contains provisions of current § 205.15, *Annual reports.* Proposed § 205.26 provides that annual reports are due to FMS on December 31 for the State's most recently completed fiscal year. Interest will continue to be exchanged on March 1 since interest liabilities are aggregated among all States to offset direct costs, as noted in proposed § 205.27. Prior period adjustments are limited to the two State

fiscal years prior to the State fiscal year covered by an annual report.

Section 205.27 How Are Direct Costs Calculated?

Proposed § 205.27 contains provisions found in current § 205.14, *Direct costs of implementation.* Provisions on cost claims for the initial implementation of CMIA are deleted. In addition, the proposed rule deletes the requirement that FMS review the policies on direct costs of implementation to determine their effectiveness. In reviewing direct cost claims for reasonableness, we will consider how necessary a task is to the development and maintenance of clearance patterns in support of interest calculations or the actual calculation of interest liabilities. All States seeking reimbursement should maintain proper documentation of accrued expenses. States seeking more than $50,000 for direct costs should have documentation supporting that assertion.

The General Accounting Office report noted that some States believe they should be reimbursed for costs that are outside the definition of direct costs for the implementation of subpart A as set forth in § 205.12. Congress authorized FMS to reimburse only those costs directly related to the interest calculations required by this Part. Congress intended that other costs should be reimbursed in accordance with Office of Management and Budget guidelines for reimbursement for indirect program costs (OMB Circular A–87). In order to clarify the scope of direct costs that are reimbursable under CMIA, the definition of direct cost in § 205.2 has been revised to provide that States will be compensated only for costs associated with the calculation of CMIA interest, including those costs a State incurs in developing and maintaining clearance patterns in support of interest calculations. The legislative history of the cost recovery provisions of CMIA was discussed in the proposed and final CMIA rules. 57 FR 10102 and 57 FR 44272.

Section 205.28 How Are Interest Payments Exchanged?

Proposed § 205.28 addresses the manner in which States and the Federal agencies offset interest liability on or before March 31 of each year. This interest exchange date is changed from March 1 in the existing regulation. The date change will benefit all stakeholders seeking an equitable exchange of interest because more time will be allowed to conduct comprehensive reviews of disputed liabilities.

Section 205.29 What Are the State Oversight and Compliance Responsibilities?

Proposed § 205.29 restates, without material change, the State oversight and compliance responsibilities that are set forth in current § 205.17, *Compliance and oversight.* A State's implementation of subpart A is subject to audit in accordance with the requirements for single audits. CMIA specific audit objectives and suggested audit procedures now appear in the *OMB Circular A–133 Compliance Supplement.* States are required to maintain all pertinent records for three fiscal years following submission of an Annual Report.

Section 205.30 What Are the Federal Oversight and Compliance Responsibilities?

The Federal oversight and compliance responsibilities that are set forth in current § 205.17, *Compliance and oversight,* are relocated to proposed § 205.30. In addition, proposed § 205.30 requires Federal agencies to notify us when they have actual or constructive knowledge that corrective action needs to be taken by us or by a State with respect to the implementation of Part 205 or if a State's clearance pattern doesn't correspond to a program's clearance activity. We believe that this requirement will improve compliance with Part 205.

Proposed § 205.30 also clarifies that Federal program agencies are responsible for determinations regarding whether or not costs should be properly chargeable to the Federal government.

Federal program agencies that incur interest liabilities through improper actions or compliance failures continue to be subject to charges by FMS. In these instances, we will issue a Notice of Assessment that describes the nature of the non-compliance and the amount of the charge to the Federal program agency. An appeals process is available to Federal program agencies.

Section 205.31 How Does a State or Federal Program Agency Appeal a Determination Made by Us and Resolve Disputes?

Proposed § 205.31 sets forth the appeal and dispute provisions that appear in current § 205.18. However, unlike the current rule, the proposed rule provides that an aggrieved party has 90 days from the date of the notice of assessment to submit a written petition if a dispute arises from the implementation or administration of subpart A. Currently there is no limitation on the amount of time an aggrieved party can take to submit a written appeal. We are proposing this change to respond to requests from Federal agencies for a time limit on filing appeals.

Proposed § 205.31 also clarifies that the appeal and dispute resolution procedures of this section apply to matters concerning the implementation of subpart A and do not apply to disputes between States and Federal program agencies concerning the determination of whether a cost is properly chargeable to the Federal government.

Subpart B: Rules Applicable to Federal Assistance Programs Not Included in a Treasury-State Agreement

Section 205.32 What Federal Assistance Programs Are Subject to Subpart B?

This section clarifies that all Federal assistance programs listed in the Catalogue of Federal Domestic Assistance, but not included in a State's Treasury-State Agreement or subject to default procedures, are subject to subpart B.

Section 205.33 How Are Funds Transfers Processed?

Proposed § 205.33 reaffirms the overall goal of Part 205, efficient cash management. Federal program agencies and States must limit funds transfers to the minimum amounts necessary to meet program goals. These funds transfers must be conducted to minimize the time between the funding and the paying out of the funds for Federal assistance program purposes.

This section states that no interest liability will be incurred by States or Federal program agencies for funds transfers subject to subpart B.

Section 205.34 What Are the Federal Oversight and Compliance Responsibilities?

Federal program agencies must monitor a State's practices and notify us if a State exhibits an unwillingness or inability to practice efficient cash management. Federal program agencies must develop procedures to comply with subpart B to promote efficient cash management.

Section 205.35 What Is the Result of Federal Program Agency or State Non-Compliance?

In the event of State or Federal program agency non-compliance, we may transfer Federal assistance programs to subpart A. These programs would then be subject to interest liabilities.

Subpart C [Reserved]

Subpart C remains reserved pending further consideration. In the Notice of Proposed Rulemaking issued in March 1992, 57 FR 10102, this section applied to programs administered by non-State recipients and non-State subrecipients. Subpart C did not apply the interest provisions of CMIA to these non-state recipients and sub-recipients and is not included in the Final Rule.

IV. Procedural Matters

Executive Order 12866, Regulatory Planning and Review

These proposed regulations are not a significant regulatory action and are not subject to review by the Office of Management and Budget under Executive Order 12866. These proposed regulations will not have effect of $100 million or more on the economy. They will not adversely affect in a material way the economy, productivity, competition, jobs, the environment, public health or safety, or State, local, or tribal governments or communities. These proposed regulations will not create a serious inconsistency or otherwise interfere with an action taken or planned by another agency. These proposed regulations do not alter the budgetary effects of entitlement, grants, user fees, or loan programs, or the right or obligations of their recipients; nor do they raise novel legal or policy issues.

Clarity of the Regulations

Executive Order 12866 requires each agency to write regulations that are simple and easy to understand. President Clinton's Presidential memorandum of June 2, 1998, requires us to write new regulations in plain language. We invite your comments on how to make these proposed regulations easier to understand.

Regulatory Flexibility Act

Pursuant to section 605(b) of the Regulatory Flexibility Act, it is hereby certified that this proposal will not have a significant economic impact on a substantial number of small business entities. The proposed rule does not require any actions on the part of small entities. Accordingly, a Regulatory Flexibility Act analysis is not required.

Paperwork Reduction Act

The Office of Management and Budget has approved the information collection requirements in the proposed rule under the Paperwork Reduction Act of 1995, 44 U.S.C. 3501 *et seq.*, and has assigned clearance number 1510–0061. Sections of this proposed rule with information collection requirements are 205.9, 205.26, 205.27, 205.29, and we estimate the public reporting burden of these sections to average, respectively, 500 hours per response. This estimate includes the time for reviewing instructions, searching existing data sources, gathering and maintaining the data needed, and completing and reviewing the collection of information. We estimate the number of respondents to be 56.

Send comments regarding this burden estimate or any other aspect of this collection of information, including suggestions for reducing the burden, to Information Collection Clearance Officer, Office of Information and Regulatory Affairs, Office of Management and Budget, New Executive Office Building, Washington, DC 20503; Attention: 1510–AA38; with copies to Juanita Holder, Public Reports Clearance Officer, Financial Management Service, 3361 75th Avenue, Landover, Maryland 20785.

List of Subjects in 31 CFR Part 205

Electronic funds transfer, Grant programs, Intergovernmental relations.

Authority and Issuance

For the reasons set out in the preamble, we propose to revise part 205 of title 31 of the Code of Regulations to read as follows:

PART 205—RULES AND PROCEDURES FOR EFFICIENT FEDERAL-STATE FUNDS TRANSFERS

Sec.

Authority: 5 U.S.C. 301; 31 U.S.C. 321, 3335, 6501, 6503.

§ 205.1 What Federal assistance programs are covered by this part?

(a) This part prescribes rules for transferring funds between the Federal Government and States for Federal assistance programs. This part applies to:

(1) All States as defined in § 205.2; and

(2) All Federal program agencies, except the Tennessee Valley Administration (TVA) and its Federal assistance programs.

(b) Only programs listed in the Catalog of Federal Domestic Assistance, as established by Chapter 61 of Title 31, United States Code (U.S.C.) are covered by this part.

(c) This part does not apply to:

(1) Payments made to States acting as vendors on Federal contracts, which are

subject to the Prompt Payment Act of 1982, as amended, 31 U.S.C. 3901 *et seq.*, 5 CFR part 1315, and 48 CFR part 32; or

(2) Direct loans from the Federal Government to States.

§ 205.2 What definitions apply to this part?

For purposes of this part:

Administrative cost grant means a grant wholly dedicated to compensate States for administrative expenses.

Administrative costs means expenses incurred by a State associated with managing a Federal assistance program.

Auditable means records must be retained to allow for calculations outlined in the Treasury-State Agreements to be reviewed and replicated for compliance purposes. States must maintain these records to be readily available, fully documented, and verifiable.

Authorized State Official means a person with the authority under the laws of a State to make commitments on behalf of the State for the purposes of this part, or that person's official designee as certified in writing.

Business day means a day when Federal Reserve Banks are open.

Catalog of Federal Domestic Assistance (CFDA) means the government-wide list of Federal assistance programs, projects, services, and activities which provide assistance or benefits to the American public. The listing includes financial and nonfinancial Federal assistance programs administered by agencies of the Federal Government. (The Catalog is available at http://www.cfda.gov)

Clearance pattern means a forecast showing the daily amount subtracted from a State's bank account each day after the State makes a disbursement. For example, a State mailing out benefit checks may forecast that the percentage of checks cashed each day will be 0% for the first day, 10% for the second day, 80% on the third day, and 10% on the fourth day following issuance. Clearance patterns are used to schedule the transfer of funds with various funding techniques and to support interest calculations.

Compensating balance means funds maintained in State bank accounts and/or State Treasurer bank accounts to offset the costs of bank services.

Current project cost means a cost for which the State has recorded a liability on or after the day that the State last requested funds for the project.

Day means a calendar day unless otherwise specified.

Default procedures means efficient cash management practices that we prescribe for Federal funds transfers to a State if a Treasury-State Agreement is not in place.

Direct cost means those costs a State incurs in performing the actual calculation of interest liabilities, including those costs a State incurs in developing and maintaining clearance patterns in support of interest calculations.

Disallowances mean costs incurred by a State which the Federal program agency has determined to be costs which should not be charged to the Federal Government either because the funds were used for other than Federal assistance program purposes or the amount of the funds used for Federal assistance program purposes was improper.

Disburse means to issue a check or initiate an electronic funds transfer payment.

Discretionary grant project means a project for which a Federal program agency is authorized by law to exercise judgment in awarding a grant and in selecting a grantee, generally through a competitive process.

Dollar-weighted average day of clearance means the day when, on a cumulative basis, 50 percent of funds have been paid out. To calculate the dollar-weighted average day of clearance for a clearance pattern:

(1) For each day, multiply the percentage of dollars paid out that day by the number of days that have elapsed since the payments were issued. For example, on the first day payments were issued, multiply the percentage of dollars paid out on that day by zero, since zero days have elapsed. On the day after payments were issued, multiply the percentage of dollars paid out on that day by one, since one day has elapsed; and so forth.

(2) Total the results from paragraph (1) of this definition. Round to the nearest whole number. This is the dollar-weighted average day of clearance.

Draw down (verb) means a process in which a State requests and receives Federal funds. *Drawdown* (noun) means Federal funds requested and received by a State.

Electronic Funds Transfer (EFT) means any transfer of funds, other than a transaction originated by cash, check, or similar paper instrument, that is initiated through an electronic terminal, telephone, computer, or magnetic tape, for the purpose of ordering, instructing, or authorizing a financial institution to debit or credit an account.

Estimate means a projection of the future needs of a Federal assistance program that can't be accurately described by a clearance pattern.

Federal assistance program means a program included in the Catalog of Federal Domestic Assistance where funds are transferred from the Federal Government to a State. Federal assistance programs do not include vendor payments or direct loans.

Federal program agency means an executive agency as defined by section 102 of title 31, United States Code, except the Tennessee Valley Authority (TVA), that issues and administers grants to States or cooperative agreements with States.

Federal-State agreement means an agreement between a State and a Federal program agency specifying terms and conditions for carrying out a Federal assistance program or group of programs. This is different than a Treasury-State Agreement.

Financial Management Service (we or us) means the Bureau of the U.S. Department of the Treasury responsible for implementation of this part.

Fiscal Year means the twelve-month period that a State designates as its budget year.

Grant means, for the purposes of this Part, a funds transfer by the Federal Government associated with a Federal assistance program listed in the Catalog of Federal Domestic Assistance.

Indirect cost means costs a State incurs that are necessary to the operation and performance of its Federal assistance programs, but that aren't readily identifiable with a particular project or Federal assistance program.

Indirect cost rate means a formula that identifies the amount of indirect costs based on the amount of accrued direct costs.

Maintenance-of-effort means a requirement that a State spend at least a specified amount of State funds for Federal assistance program purposes.

Major Federal assistance program means a Federal assistance program which receives Federal funding in excess of the dollar thresholds found in Table A to § 205.5.

Obligational authority means the existence of a definite commitment on the part of the Federal Government to provide appropriated funds to a State to carry out specified programs, whether the commitment is executed before or after a State pays out funds for Federal assistance program purposes.

Pay out means to debit the State's bank account.

Pay out funds for Federal assistance program purposes means, in the context of State payments, to debit a State account for the purpose of making a payment properly chargeable to the Federal Government to:

(1) A person or entity that is not considered part of the State pursuant to the definition of ''State'' in this section; or

(2) A State entity that provides goods or services for the direct benefit or use of the payor State entity or the Federal Government to further Federal assistance program goals.

Rebate means funds returned to a State by third parties after a State has paid out those funds for Federal assistance program purposes.

Refund means funds that a State recovers that it previously paid out for Federal assistance program purposes. Refunds include rebates received from third parties.

Refund transaction means an entry to the record of a State bank account representing a single deposit of refunds. A refund transaction may consist of a single check or item, or a bundle of accumulated checks.

Related banking costs means separately identified costs which are necessary and customary for maintaining an account in a financial institution, whether a commercial account or a State Treasurer account. Investment service fees and fees for credit-related services aren't related banking costs.

Request for funds means a State's request for funds that the State completes and submits in accordance with Federal program agency guidelines.

Reverse flow program means a Federal assistance program, such as Supplemental Security Income (SSI), for which the Federal Government makes payments to recipients on behalf of a State.

Revolving loan fund means a pool of program funds managed by a State. States may loan funds from the pool to other entities in support of Federal assistance program goals. Investment income is earned on the funds that remain in the pool and on loans made from pool funds. A Federal program agency may require that all income derived from a revolving loan fund be used for Federal assistance program purposes.

Secretary means the Secretary of the United States Department of the Treasury. We are the Secretary's representative in all matters concerning this Part, unless otherwise specified.

State means a State of the United States, the District of Columbia, the Commonwealth of Puerto Rico, the Commonwealth of the Northern Mariana Islands, American Samoa, Guam, and the Virgin Islands. It includes any agency, instrumentality, or fiscal agent of a State that is legally and fiscally dependent on the State executive, State Treasurer, or State Comptroller.

(1) A State agency or instrumentality is any organization of the primary government of the State financial reporting entity, as defined by generally accepted accounting principles.

(2) A fiscal agent of a State is an entity that pays, collects, or holds Federal funds on behalf of the State in furtherance of a Federal assistance program, excluding private nonprofit community organizations.

(3) Local governments, Indian Tribal governments, institutions of higher education, hospitals, and nonprofit organizations are excluded from the definition of State.

Treasury-State Agreement means a document describing the accepted funding techniques and methods for calculating interest and identifying the Federal assistance programs governed by this subpart A.

Trust fund for which the Secretary is the trustee means a trust fund administered by the Secretary.

Vendor payment means a funds transfer by a Federal program agency to a State to compensate the State for acting as a vendor on a Federal contract.

We and us means Financial Management Service.

Subpart A—Rules Applicable to Federal Assistance Programs Included in a Treasury-State Agreement

§ 205.3 What Federal assistance programs are subject to this subpart A?

(a) Generally, this subpart prescribes the rules that apply to Federal assistance programs which:

(1) Are listed in the Catalog of Federal Domestic Assistance;

(2) Meet the funding threshold for a major Federal assistance program; and

(3) Are included in a Treasury-State Agreement or default procedures.

(b) Upon a State's request, we will make additional Federal assistance programs subject to this subpart A by lowering the funding threshold in the Treasury-State Agreement. All of a State's programs that meet this lower threshold would be subject to this subpart A.

(c) We may make additional Federal assistance programs subject to this subpart A if a State or Federal program agency fails to comply with subpart B of this part.

§ 205.4 Are there any circumstances where a Federal assistance program that meets the criteria of § 205.3 would not be subject to this subpart A?

(a) A Federal assistance program that meets or exceeds the threshold for major Federal assistance programs in a State is not subject to this subpart A until it is included in an amended Treasury-State Agreement or in default procedures.

(b) We and a State may agree to exclude components of a major Federal assistance program from interest calculations if the State administers the program through several State agencies and meets the following requirements:

(1) The dollar amount of the exempted cash flow doesn't exceed 5% of the State's major Federal assistance program threshold and can't exceed 10% of that Federal assistance program's total expenditures;

(2) If less than the total amount of Federal assistance program funding is subject to interest calculation procedures, the interest liabilities should be pro-rated to 100% of the Federal assistance program funding;

(3) A State may not use this exclusion if a Federal assistance program is administered by only one State agency; and

(4) We may request Federal assistance program specific data on funding levels to determine exemptions.

(c) We and a State may exclude a Federal assistance program from this subpart A if the Federal assistance program has been discontinued since the most recent Single Audit and the remaining funding is below the threshold, or if the Federal assistance program is funded by an award not limited to one fiscal year and the remaining Federal assistance program funding is below the State's threshold.

§ 205.5 What are the thresholds for major Federal assistance programs?

(a) Table A of this section defines major Federal assistance programs based on the dollar amount of an individual Federal assistance program and the dollar amount of all Federal assistance being received by a State for all Federal assistance programs. A State must locate the appropriate row in Column A based upon the total expenditures of Federal assistance received. In that same row, a State must apply the percentage from Column B to determine the State's threshold for major Federal assistance programs. A State with expenditures greater than $10 billion will have a minimum default threshold of $60 million.

(b) To ensure adequate coverage of all State programs, a State must compare its program coverage using the threshold figure obtained under paragraph (a) of this section to the program coverage projected by a threshold of one half that of paragraph (a) of this section.

(1) Sum the total dollar expenditures of programs that exceed the threshold

determined in Column B. Designate this amount as X.

(2) Sum the total dollar expenditures of programs that exceed one half of the threshold amount determined in Column B. Designate this amount as Y.

(3) Subtract X from Y. Designate this amount as Z.

(4) If Z is less than or equal to 10% of Y use the figure found in Column B of Table A.

(5) If Z is greater than 10% of Y, then a State must lower its threshold, or add programs, until the difference between Y and the new total dollar value of program coverage is less than or equal to 10%.

(c) Unless specified otherwise, major Federal assistance programs must be determined from the most recent Single Audit data available.

TABLE A TO § 205.5

Column A—Total expenditure of Federal Assistance for all programs per State	Column B—Major Federal Assistance Program means any Federal assistance program with expenditures that exceed these levels
Between zero and $100 million inclusive	6.00 percent of such total expenditures.
Over $100 million but less than or equal to $10 billion	0.60 percent of such total expenditures.
Over $10 billion	The greater of 0.30 percent of such total expenditures or $60 million.

§ 205.6 What is a Treasury-State Agreement?

(a) A Treasury-State Agreement documents the accepted funding techniques and methods for calculating interest agreed upon by us and a State and identifies the Federal assistance programs governed by this subpart A. If anything in a Treasury-State Agreement is inconsistent with this subpart A, that part of the Treasury-State Agreement won't have any effect and this subpart A will govern.

(b) A Treasury-State Agreement will be effective until terminated. We or a State may terminate a Treasury-State Agreement on 30 days written notice.

§ 205.7 Can a Treasury-State Agreement be amended?

(a) We or a State may amend a Treasury-State Agreement at any time if both we and the State agree in writing.

(b) The effective date of an amendment shall be the date both parties agree to the amendment in writing. Amendments may not be retroactive, except for an amendment to clarify the terms of a Treasury-State Agreement.

(c) We and a State must amend a Treasury-State Agreement as needed to change or clarify its language when the terms of the existing agreement are either no longer correct or no longer applicable. A State must notify us in writing describing the Federal assistance program change and include a proposed amendment for our review and a current list of all programs included in the Treasury-State Agreement. Amendments may address, but are not limited to:

(1) Additions or deletions of Federal assistance programs subject to this subpart A;

(2) Changes in funding techniques; and

(3) Changes in clearance patterns.

(d) Additions or deletions to the list of Federal assistance programs subject to this subpart A take effect when a Treasury-State Agreement is amended.

(e) Federal assistance programs that are to be added to a Treasury-State Agreement are not subject to this subpart A until the Treasury-State Agreement is amended, except when a Federal assistance program subject to this subpart A is being replaced by a Federal assistance program governed by subpart B of this part, in which case the replacement program is immediately subject to this subpart A.

§ 205.8 What if there is no Treasury-State Agreement in effect?

When a State doesn't have a Treasury-State Agreement in effect, we will prescribe default procedures to implement this subpart A. The default procedures will prescribe efficient funds transfer procedures consistent with State and Federal law and identify the covered Federal assistance programs and designated funding techniques.

§ 205.9 What is included in a Treasury-State Agreement?

We will prescribe a uniform format for all Treasury-State Agreements. A Treasury-State Agreement must include, but is not limited to, the following:

(a) State agencies, instrumentalities, and fiscal agents that administer the Federal assistance programs subject to this subpart A.

(b) Federal assistance programs subject to this subpart A, consistent with §§ 205.3 and 205.4. A State must use its most recent single audit report as a basis for determining the funding thresholds for major Federal assistance programs, unless otherwise specified in the Treasury-State Agreement. A State may use budget or appropriations data for a more recent period instead of single audit data, if specified in the Treasury-State Agreement.

(c) Funding techniques applied to Federal assistance programs subject to subpart A based on the Federal assistance program's purpose and administration.

(d) Methods the State will use to develop and maintain clearance patterns and estimates, consistent with § 205.11. The method must include, at a minimum, a clear indication of:

(1) the data used;

(2) the sources of the data;

(3) the development process;

(4) for estimates, when and how the State will update the estimate to reflect the most recent data available;

(5) for estimates, when and how the State will make adjustments, if any, to reconcile the difference between the estimate and the State's actual cash needs; and

(6) any assumptions, standards, or conventions used in converting the data into the clearance pattern or estimate.

(e) Federal program agency provisions requiring reconciliation of estimates to actual outlays may be included in a Treasury-State Agreement. The supporting documentation must be retained by the State for three years.

(f) States must include the results of the clearance pattern process in the Treasury-State Agreement. The supporting documentation must be retained by the State for three years.

(g) Methods used by the State and Federal agencies to calculate interest liabilities pursuant to this subpart A. The method must include, but is not limited to, a clear indication of:

(1) the data used;

(2) the sources of the data;

(3) the calculation process; and

(4) any assumptions, standards, or conventions used in converting the data into the interest liability amounts.

(h) Treasury-State agreements must include language describing how a State and Federal program agency will address a State request for supplemental funding. This language must include, but is not limited to, the following provisions:

(1) What constitutes a timely request for supplemental funds for Federal assistance program purposes by a State; and

(2) What constitutes a timely transfer of supplemental funds for Federal assistance program purposes from a Federal program agency to a State.

§ 205.10 How do you document funding techniques?

The Treasury-State Agreement must include a concise description for each funding technique that a State will use. The description must include the following:

(a) What constitutes a timely request for funds;

(b) How the State determines the amount of funds to request;

(c) What procedures are used to estimate or reconcile estimates with actual and immediate cash needs;

(d) What constitutes the timely receipt of funds; and

(e) Whether a State or Federal interest liability accrues when the funding technique, including any associated procedure for estimation or reconciliation, is properly applied.

§ 205.11 What requirements apply to funding techniques?

(a) A State and a Federal program agency must minimize the time elapsing between the transfer of funds from the United States Treasury and the State's pay out of funds for Federal assistance program purposes, whether the transfer occurs before or after the pay out of funds.

(b) A State and a Federal program agency must limit the amount of funds transferred to the minimum required to meet a State's actual and immediate cash needs.

(c) A State must not draw down funds from its account in the Unemployment Trust Fund or from a Federal account in the Unemployment Trust Fund in advance of actual immediate cash needs for any purpose including maintaining a compensating balance.

(d) A Federal program agency must allow a State to submit requests for funds daily. This requirement shouldn't be construed as a change to Federal program agency guidelines defining a properly completed request for funds.

(e) In accordance with the electronic funds transfer provisions of the Debt Collection Improvement Act of 1996 (31 U.S.C. 3332), a Federal program agency must use electronic funds transfer methods to transfer funds to States unless a waiver is available.

§ 205.12 What funding techniques may be used?

(a) We and a State may negotiate the use of mutually agreed upon funding techniques. We may deny interest liability if a State does not use a mutually agreed upon funding technique. Funding techniques should be efficient and minimize the exchange of interest between States and Federal agencies.

(b) We and a State may base our agreement on the sample funding techniques listed in paragraphs (b)(1) through (5) of this section, or any other technique upon which both parties agree.

(1) Zero balance accounting means that a Federal program agency transfers the actual amount of Federal funds to a State that are paid out by the State each day.

(2) Estimated clearance means that a Federal program agency transfers to a State the estimated amount of funds that the State pays out each day. The estimated amount paid out each day is determined by applying a clearance pattern to the total amount the State will disburse.

(3) Average clearance means that a Federal program agency, on the dollar-weighted average day of clearance of a disbursement, transfers to a State a lump sum equal to the actual amount of funds that the State is paying out. The dollar-weighted average day of clearance is the day when, on a cumulative basis, 50 percent of the funds have been paid out. The dollar-weighted average day of clearance is calculated from a clearance pattern, consistent with § 205.20.

(4) Cash advance (preissuance) funding means that a Federal program agency transfers the actual amount of Federal funds to a State that will be paid out by the State, in a lump sum, not more than 2 business days prior to the day the State issues checks or initiates EFT payments.

(5) Reimbursable funding means that a Federal program agency transfers Federal funds to a State after that State has already paid out the funds for Federal assistance program purposes.

§ 205.13 How do you determine when State or Federal interest liability accrues?

(a) State or Federal interest liability may or may not apply when mutually agreed to funding techniques are applied, depending on the terms of the Treasury-State Agreement.

(b) We and a State may agree in a Treasury-State Agreement that no State or Federal interest liability will accrue for indirect costs or indirect allocated costs based on an indirect cost rate. This indirect cost rate must be approved by the appropriate Federal program agency under Office of Management and Budget (OMB) Circular A–87 (available from the addresses in 5 CFR 1310.3) and be in accordance with this subpart A.

§ 205.14 When does Federal interest liability accrue?

(a) Federal interest liabilities may accrue if funding techniques aren't properly applied, in accordance with the following provisions:

(1) The Federal program agency incurs interest liability if a State pays out its own funds for Federal assistance program purposes with valid obligational authority under Federal law, Federal regulation, or Federal-State agreement. A Federal interest liability will accrue from the day a State pays out its own funds for Federal assistance program purposes to the day Federal funds are credited to a State account.

(2) If a State pays out its own funds for Federal assistance program purposes without obligational authority, the Federal program agency incurs an interest liability if obligational authority subsequently is established.

(3) If a State pays out its own funds prior to the day a Federal program agency officially notifies the State in writing that a discretionary grant project is approved, the Federal program agency doesn't incur an interest liability, notwithstanding any other provision of this section.

(4) If a State pays out its own funds prior to the availability of Federal funds authorized or appropriated for a future Federal fiscal year, the Federal program agency doesn't incur an interest liability, notwithstanding any other provision of this section.

(5) If a State fails to request funds timely as set forth in § 205.29 or otherwise fails to apply a funding technique properly, we may deny any resulting Federal interest liability.

(b) Federal agency programs that have specific payment dates set by the Federal program agency that create interest liabilities are subject to this part.

(c) States must adhere to Federal program agency disbursement schedules when requesting funds. We may deny a State's claim for Federal interest liability for the period prior to a late drawdown request. States must time their funds drawdown so that it does not create Federal interest liability. The drawdown request must allow the Federal program agency sufficient time to meet its disbursement schedule. If the Federal program agency does not make a timely payout in accordance with the terms of the Treasury-State Agreement,

a State may submit a claim for interest liability.

§ 205.15 When does State interest liability accrue?

(a) *General rule.* State interest liability may accrue if Federal funds are received by a State prior to the day the State pays out the funds for Federal assistance program purposes. State interest liability accrues from the day Federal funds are credited to a State account to the day the State pays out the Federal funds for Federal assistance program purposes.

(b) *Disallowances.* A State incurs an interest liability on disallowances.

(1) If a Federal program agency disallows a State expenditure, a State will owe interest from the day that Federal funds associated with the disallowance are credited to a State account to the day the funds are credited to the Federal government.

(2) In instances where an expenditure is disallowed in a CMIA reporting year subsequent to the CMIA reporting year in which the State made the expenditure, the amount of interest calculated in accordance with paragraph (b)(1) of this section shall be adjusted for any CMIA interest previously paid on such amounts, either by a State or by the Federal government.

(c) *Refunds.* (1) A State incurs interest liability on refunds of Federal funds from the day the refund is credited to a State account to the day the refund is either paid out for Federal assistance program purposes or credited to the Federal government.

(2) We and a State may agree, in a Treasury-State Agreement, that a State doesn't incur an interest liability on refunds in refund transactions under $50,000.

(d) *Exception to the general rule.* A State does not incur an interest liability to the Federal Government if a Federal statute requires the State to retain or use for Federal assistance program purposes the interest earned on Federal funds, notwithstanding any other provision in this section.

§ 205.16 What special rules apply to Federal assistance programs and projects funded by the Federal Highway Trust Fund?

The following applies to Federal assistance programs and projects funded out of the Federal Highway Trust Fund, notwithstanding any other provision of this part:

(a) A State must request funds at least weekly for current project costs, or Federal interest liability won't accrue prior to the day a State submits a request for funds.

(b) If a State pays out its own funds in the absence of a project agreement or in excess of the Federal obligation in a project agreement, the Federal program agency won't incur an interest liability.

§ 205.17 Are funds transfers delayed by automated payment systems restrictions based on the size and timing of the drawdown request subject to this part?

Funds transfers delayed due to payment processes that automatically reject drawdown requests that fall outside a pre-determined set of parameters are subject to this part.

§ 205.18 Are Federal assistance program agency grants for administrative costs subject to this part?

(a) Federal assistance program agency grants wholly dedicated to compensate States for administrative costs are subject to this part.

(b) Federal assistance program agency grants dedicating only a portion of their funding for administrative costs are partially exempt from this part. The portion dedicated to compensate States for indirect and other administrative costs is not subject to this part.

§ 205.19 How is interest calculated?

(a) A State must calculate Federal interest liabilities and State interest liabilities for each Federal assistance program subject to this subpart A.

(b) The interest rate for all interest liabilities for each Federal assistance program subject to subpart A is the annualized rate equal to the average equivalent yields of 13-week Treasury Bills auctioned during a State's fiscal year. We provide this rate to each State.

(c) A State must calculate and report interest liabilities on the basis of its fiscal year. A State must ensure that its interest calculations are auditable and retain a record of the calculations.

(d) As set forth in § 205.9, a Treasury-State Agreement must include the method a State uses to calculate and document interest liabilities.

(e) A State may use actual data, a clearance pattern, or statistical sampling to calculate interest. A clearance pattern used to calculate interest must meet the standards of § 205.20. If a State uses statistical sampling to calculate interest, the State must sample transactions separately for each Federal assistance program subject to this subpart A. Each sample must be representative of the pool of transactions and be of sufficient size to accurately represent the flow of Federal funds under the Federal assistance program, including seasonal or other periodic variations.

(f) For the first year in which a Federal assistance program is covered in a Treasury-State Agreement, funds transfers that occur prior to the first day of the State's fiscal year must not be included in interest calculations and are not subject to the interest liability provisions of this part.

§ 205.20 What is a clearance pattern?

States use clearance patterns to estimate when funds are paid out, given a known dollar amount and a known date of disbursement. We and a State may agree to other procedures to estimate when funds are paid out when the dollar amount and/or the timing of disbursements are not known. A State must ensure that clearance patterns meet the following standards:

(a) A clearance pattern must be auditable.

(b) A clearance pattern must accurately represent the flow of Federal funds under the Federal assistance programs to which it is applied.

(c) A clearance pattern must include seasonal or other periodic variations in clearance activity.

(d) A clearance pattern must be based on at least three consecutive months of disbursement data, unless additional data is required to accurately represent the flow of Federal funds.

(e) If a State uses statistical sampling to develop a clearance pattern, the sample size must be sufficient to ensure a 96% confidence interval no more than plus or minus 0.25 weighted days above or below the estimated mean.

(f) A clearance pattern must extend, at a minimum, until 99 percent of the dollars in a disbursement have been paid out for Federal assistance program purposes.

§ 205.21 When may clearance patterns be used?

(a) A State may develop a clearance pattern for:

(1) An individual Federal assistance program;

(2) A logical group of Federal assistance programs that have the same disbursement method and type of payee;

(3) A bank account;

(4) A specific type of payments, such as payroll or vendor payments; or

(5) Anything that is agreed upon by us and a State. If a clearance pattern is used for multiple Federal assistance programs, a State must apply the clearance pattern separately to each Federal assistance program when scheduling funds transfers or calculating interest.

(b) As set forth in § 205.9, a Treasury-State Agreement must include the method a State uses to develop and maintain clearance patterns.

§ 205.22 How are accurate clearance patterns maintained?

(a) If a State has knowledge, at any time, that a clearance pattern no longer

reflects a Federal assistance program's actual clearance activity, or if a Federal assistance program undergoes operational changes that may affect clearance activity, the State must notify us, develop a new clearance pattern, and certify that the new pattern corresponds to the Federal assistance program's clearance activity.

(b) An authorized State official must certify that a clearance pattern corresponds to the clearance activity of the Federal assistance programs to which it is applied. An authorized State official must re-certify the accuracy of a clearance pattern at least every 5 years. If a State develops a clearance pattern for a bank account or a specific type of payment, or on another basis, as set forth in § 205.21, we may prescribe other requirements for re-certifying the accuracy of the clearance pattern. A State can begin to use a new clearance pattern on the date the new clearance pattern is certified.

§ 205.23 What requirements apply to estimates?

The requirements in this section apply when we and a State negotiate a mutually agreed upon funds transfer procedure based on an estimate of the State's immediate cash needs. These requirements don't apply to an estimate based on a clearance pattern or an indirect cost rate.

(a) The State must ensure that the estimate reasonably represents the flow of Federal funds under the Federal assistance program or program component to which the estimate applies. The estimate must take into account seasonal or other periodic variations in activity throughout the period for which the Federal funds are available. If a State supplements the Federal funds for a Federal assistance program, other than through required matching, the State must not arbitrarily assign its earliest costs to the Federal Government. The State may allocate its costs proportionately over the period for which the Federal funds are available, or specify in the Treasury-State Agreement which Federal assistance program components will use Federal funds exclusively.

(b) As set forth in § 205.9, a Treasury-State Agreement must include the method a State uses to develop and maintain the estimate.

§ 205.24 How are accurate estimates maintained?

(a) If a State has knowledge that an estimate doesn't reasonably correspond to the State's cash needs for a Federal assistance program or program component, or if a Federal assistance program undergoes operational changes that may affect cash needs, the State must immediately notify us in writing. We and the State will amend the funding technique provisions in the Treasury-State Agreement or take other mutually agreed upon corrective action.

(b) When estimates are properly updated and applied, a State or Federal interest liability may or may not accrue, depending on the terms of the Treasury-State Agreement.

(c) We may require a State to justify in writing that it is not feasible to use a more efficient funding technique for the Federal assistance program or program component to which an estimate is applied. We may prescribe requirements for certifying the reasonableness of an estimate.

§ 205.25 How does this part apply to certain Federal assistance programs or funds?

(a) Special rules apply to certain Federal assistance programs or funds described in this section. To the extent the provisions of this section are inconsistent with other provisions of this part, this section applies.

(b) A State's interest liability on funds withdrawn from its account in the Unemployment Trust Fund equals the actual interest earned on such funds less the related banking costs. Actual interest earned doesn't include non-cash bank earnings. If funds withdrawn from the State account in the UTF are commingled with other funds, the funds withdrawn from the State account must be allocated a proportionate share of interest earnings and banking costs. (Interest liabilities on funds withdrawn from a Federal account in the UTF, except the Federal Unemployment Account, are calculated in accordance with § 205.19.)

(c) Supplemental Security Income. (1) The Federal Government incurs an interest liability from the day State funds are credited to the Federal Government's account to the day a Federal program agency pays out the State funds for Federal assistance program purposes. A State incurs an interest liability from the day a Federal program agency pays out Federal funds for Federal assistance program purposes to the day State funds are credited to the Federal Government's account.

(2) Interest liability must be calculated on the difference between a State's monthly Supplemental Security Income payment and the State's actual liability for the month.

(3) The Federal Government won't incur interest liabilities on refunds of State funds under the Supplemental Security Income Program.

(4) Administrative fees charged by the Social Security Administration to States under the Supplemental Security Income program are not subject to this part.

(5) Supplemental State payments made in conjunction with Supplemental Security Income are not subject to this part.

(d) Funds collected under the Child Support Enforcement Program. (1) Funds collected by States from absent parents pursuant to Title IV–D of the Social Security Act are not subject to this part.

(2) Interest earned by States on undistributed collections must be treated as Federal assistance program income under 45 CFR 304.50(b) and is not subject to this part.

(3) Late payment fees collected by States from absent parents are not subject to CMIA interest liabilities and are not subject to this Part. However, such fees must be treated as Federal assistance program income in accordance with 45 CFR 302.75(b)(6).

(e) States supplementing Social Services block grants, Temporary Assistance for Needy Families block grants, and the Mandatory and Matching Child Care Funds program. (1) At the discretion of the Office of Management and Budget, Federal funds will be apportioned to avoid depletion and a supplemental appropriation.

(2) A State must not draw down all Federal funds prior to spending State funds.

(3) A State is entitled to interest if the apportioned funds are not transferred timely.

(4) A State that provides matching State funding and/or maintenance-of-effort funding, as defined in 45 CFR 98.60(f), in conjunction with a Federal block grant program:

(i) Must not arbitrarily assign its earliest costs to the Federal Government;

(ii) Must coordinate a proportional drawdown of State and Federal funds to avoid interest liabilities; and

(iii) Must include these arrangements in the Treasury-State Agreement.

(f) A State that earns interest on Special Supplemental Food Program for Women, Infants, and Children rebates is not subject to interest liability if the funds earned are used for Federal assistance program purposes.

(g) Revolving Loan Funds. (1) This part applies to any transfer of funds from the Federal program agency to the State for the Revolving Loan Fund.

(2) This part doesn't apply to interest a State earns on Revolving Loan Funds when Federal program agency regulations require that all interest

earned on invested funds be used for Federal assistance program purposes.

§ 205.26 What are the requirements for creating Annual Reports?

(a) A State must submit to us an Annual Report accounting for the interest liabilities of the State's most recently completed fiscal year. Adjustments to the Annual Report must be limited to the two State fiscal years prior to the State fiscal year covered by the report. The authorized State official must certify the accuracy of a State's Annual Report. A signed original of the Annual Report must be received by the next December 31 after the end of the State's fiscal year. We will provide copies of Annual Reports to Federal agencies. We will prescribe the format of the Annual Report, and may prescribe that the Annual Report be submitted by electronic means.

(b) A State must submit a description and supporting documentation for liability claims greater than $5,000. This information must include the following:

(1) The amount of funds requested;

(2) The date the funds were requested;

(3) The date the funds were paid out for Federal assistance program purposes;

(4) The date the funds were received by the State; and

(5) The date of late grant awards.

(c) A State may submit with its Annual Report a claim for reimbursement of the direct costs of implementing this subpart A, calculated in accordance with § 205.27. An authorized State official must certify the accuracy of a State's direct cost claim.

§ 205.27 How are direct costs calculated?

(a) We will compensate a State annually for the direct costs of implementing this subpart A, subject to the conditions and limitations of this section.

(b) We may deny a direct cost claim if a State doesn't:

(1) Have a Treasury-State Agreement with us, as set forth in §§ 205.6 through 205.9;

(2) Submit timely a Treasury-State Agreement, as set forth in §§ 205.6 through 205.9;

(3) Submit timely an updated list of Federal assistance programs subject to this subpart A, as set forth in §§ 205.6 through 205.9;

(4) Submit timely a claim for direct costs with its Annual Report, as set forth in § 205.26; or

(5) Submit timely its Annual Report, as set forth in § 205.26.

(c) A State must maintain documentation to substantiate its claim for direct costs. We may require a State to provide documentation to support its direct cost claims. We will review all direct cost claims for reasonableness. If we determine that a cost claim is unreasonable, we will not reimburse a State for that cost, notwithstanding any other provision of this section.

(d) Eligibility and treatment of direct costs. (1) Direct costs don't include expenses for normal disbursing services, such as processing checks or maintaining records for accounting and reconciliation of cash accounts, or expenses for upgrading or modernizing accounting systems.

(2) Direct costs in excess of $50,000 in any year are not eligible for reimbursement, unless a State can justify to us that the State is unable to develop and maintain clearance patterns in support of interest calculations, or perform the actual calculation of interest, without incurring such costs. Supporting documentation must accompany State requests for reimbursement in excess of $50,000.

(3) Direct costs that a State incurs in fiscal years prior to its most recently completed Annual Report are not eligible for reimbursement.

(4) A State must not include the direct costs of implementing this subpart A in its State-wide cost allocation plan, as defined and provided for in OMB Circular A–87. All costs incurred by a State to implement this subpart A, other than direct costs, are subject to the procedures and principles of OMB Circular A–87.

(e) The payments from the Federal Government to individual States to offset direct costs incurred are funded from the aggregate interest payments States make to the Federal Government. The following limitations apply:

(1) We will not reduce or adjust interest liabilities for Federal assistance programs funded out of trust funds for which the Secretary is trustee; and

(2) The aggregate payments from the Federal Government to States to offset direct costs will not be greater than the aggregate interest payments States make to the Federal Government.

§ 205.28 How are interest payments exchanged?

(a) We adjust a State's total interest liability to the Federal government and the Federal government's total interest liability to a State to determine direct cost reimbursement, as set forth in § 205.27.

(b) The adjusted total State interest liability and the adjusted total Federal interest liability for each State are offset to determine the net interest payable to or from each specific State. The payment of net interest to or from a State for its most recently completed fiscal year must occur no later than March 31. We will notify a State of the final net interest liability. A State must submit a claim to receive payment.

(c) A State may appeal a decision by us on interest liabilities and direct cost claims in accordance with § 205.31.

(d) If a State appeals the amount of interest payable in accordance with the provisions of § 205.31, payment must occur by March 31 for any portions not subject to the appeal.

§ 205.29 What are the State oversight and compliance responsibilities?

(a) A State must designate an official representative with the statutory or administrative authority to coordinate all interaction with the Federal Government concerning subpart A, and must notify us in writing of the representative's name and title.

(b) A State must maintain records supporting interest calculations, clearance patterns, direct costs, and other functions directly pertinent to the implementation and administration of this subpart A for audit purposes. A State must retain the records for each fiscal year for three years from the date the State submits its Annual Report, or until any dispute or action involving the records and documents is completed, whichever is later. We, the Comptroller General, and the Inspector General or other representative of a Federal program agency must have the right of access to, and may require submission of, all records for the purpose of verifying interest calculations, clearance patterns, direct cost claims, and the State's accounting for Federal funds.

(c) A State's implementation of subpart A is subject to audit in accordance with chapter 75 of title 31, United States Code, ''Requirements for Single Audits.''

(d) If a State repeatedly or deliberately fails to request funds in accordance with the procedures established for its funding techniques, as set forth in § 205.11, § 205.12, or a Treasury-State Agreement, we may deny the State payment or credit for the resulting Federal interest liability, notwithstanding any other provision of this part.

(e) If a State materially fails to comply with this subpart A, we may, in addition to the action described in paragraph (d) of this section, take one or more of the following actions, as appropriate under the circumstances:

(1) Request a Federal program agency or the General Accounting Office to conduct an audit of the State to determine interest owed to the Federal

Government, and to implement procedures to recover such interest;

(2) Deny the reimbursement of all or a part of the State's direct cost claim;

(3) Initiate a debt collection process to recover claims owed to the United States; or

(4) Take other remedies legally available.

§ 205.30 What are the Federal oversight and compliance responsibilities?

(a) A Federal program agency must designate an official representative to coordinate all interaction with us and the States concerning this subpart A, and must notify us in writing of the representative's name and title.

(b) Determinations regarding whether or not costs are properly chargeable to the Federal government shall be the responsibility of the Federal program agency responsible for the Federal assistance program under which the disallowance arose. Disallowances will be determined in accordance with the statutes, regulations, and policies otherwise applicable to the Federal assistance program under which the disallowance arose.

(c) A Federal program agency's implementation of this subpart A is subject to review pursuant to procedural instructions that we issue.

(d) We will consult with Federal agencies as necessary and appropriate before entering into or amending a Treasury-State Agreement.

(e) We will distribute Annual Reports to Federal agencies, as set forth in § 205.26. Upon our request, a Federal program agency must review a State's Annual Report for reasonableness and must report its findings to us within 10 days.

(f) A Federal program agency must notify us in writing if the program agency has knowledge, at any time, that:

(1) A State's clearance pattern doesn't correspond to a Federal assistance program's clearance activity; or

(2) Corrective action needs to be taken by a State, us, or another Federal program agency, with respect to the implementation of this subpart. We will notify the State or Federal program agency as appropriate in writing with a description of the Federal program agency's claim.

(g) If a Federal program agency incurs an interest liability by failing to comply with this subpart A, we may collect a charge from the Federal program agency. A Federal interest liability resulting from circumstances beyond the control of a Federal program agency doesn't constitute noncompliance. We will determine the charge using the following procedures:

(1) We will issue a Notice of Assessment to the Federal program agency, indicating the nature of the noncompliance, the amount of the charge, the manner in which it was calculated, and the right to file an appeal.

(2) To the maximum extent practicable, a Federal program agency must pay a charge for noncompliance out of appropriations available for the Federal program agency's operations and not from the Federal program agency's program funds.

(3) If a Federal program agency doesn't pay a charge for noncompliance within 45 days after receiving a Notice of Assessment, we will debit the appropriate Federal program agency account.

(4) In the event a Federal program agency appeals a charge imposed under the Notice of Assessment, we will defer the charge until we decide the appeal. If we deny the appeal, the effective date of the charge may be retroactive to the date indicated in the Notice of Assessment.

§ 205.31 How does a State or Federal program agency appeal a determination made by us and resolve disputes?

(a) This section documents the procedures for:

(1) A State to appeal the net interest charge that we have assessed;

(2) A State to appeal a determination we have made regarding the State's claim for direct costs in accordance with § 205.27;

(3) A Federal program agency to appeal a charge for noncompliance that we have assessed in accordance with § 205.30; or

(4) A State or a Federal program agency to resolve other disputes with us or between or among each other concerning the implementation of this subpart A.

(b) A State or Federal program agency must submit a written petition to the Assistant Commissioner, Federal Finance, Financial Management Service (Assistant Commissioner), within 90 days of the date of the notice of assessment or the event that initiated the appeal or dispute. The Petition must include a concise factual statement, not to exceed 15 pages, with supporting documentation in the appendices, of the conditions forming the basis of the Petition and the action requested of the Assistant Commissioner. In the case of a dispute, the party submitting the petition to us must concurrently provide a copy of the petition to the other concerned parties. The other concerned parties may submit to the Assistant Commissioner a rebuttal within 90 days of the date of the petition. The rebuttal must include a concise factual statement, not to exceed 15 pages, with supporting documentation in the appendices.

(c) The Assistant Commissioner will review the Petition, any rebuttal, and all supporting documentation. As part of the review process, the Assistant Commissioner may request to meet with any or all parties and may request additional information.

(d) The Assistant Commissioner will issue a written decision within the later of 120 days of the date of the Petition, or the rebuttal in case of a dispute, or 120 days from receipt of any additional information. The Assistant Commissioner's decision will be the final program agency action on our part for purposes of judicial review procedures under the Administrative Procedures Act (APA), 5 U.S.C. 701–706, unless either the State or Federal program agency invokes the provisions of the Administrative Dispute Resolution Act of 1990 (ADRA), 5 U.S.C. 581–593.

(e) Either a State or Federal program agency may seek to invoke the provisions of the ADRA within 45 days after the date of the Assistant Commissioner's written decision.

(1) The party invoking the ADRA must notify the Assistant Commissioner and any other concerned parties in writing. If all parties, including the Assistant Commissioner, agree in writing, a neutral party appointed under the provisions of the ADRA may assist in resolving the dispute through the use of alternate means of dispute resolution as defined in the ADRA.

(2) If the party invoking the ADRA is unable to reach a satisfactory resolution, the Assistant Commissioner's decision will be the final agency action on our part for purposes of the judicial review procedures under the APA.

(f) Any amount due as a result of an appeal or dispute must be paid within 14 days of the date of the decision of the Assistant Commissioner or the date of the resolution under the ADRA. If a State fails to pay, the State will be subject to collection techniques under 31 U.S.C. 3701 *et seq.*, including accrual of interest on outstanding balances and administrative offset.

(g) The appeal and dispute resolution procedures described in this section do not apply to disputes between States and Federal program agencies concerning whether or not costs are properly chargeable to the Federal government.

Subpart B—Rules Applicable to Federal Assistance Programs Not Included in a Treasury-State Agreement

§ 205.32 What Federal assistance programs are subject to this subpart B?

This subpart B applies to all Federal assistance programs listed in the Catalog of Federal Domestic Assistance that are not subject to subpart A of this part.

§ 205.33 How are funds transfers processed?

(a) A Federal program agency must limit a funds transfer to a State to the minimum amounts needed by the State and must time the disbursement to be in accord with the actual, immediate cash requirements of the State in carrying out a Federal assistance program or project. The timing and amount of funds transfers must be as close as is administratively feasible to a State's actual cash outlay for direct program costs and the proportionate share of any allowable indirect costs.

(b) Neither a State nor the Federal government will incur an interest liability under this part on the transfer of funds for a Federal assistance program subject to this subpart B.

§ 205.34 What are the Federal oversight and compliance responsibilities?

(a) A Federal program agency must review the practices of States as necessary to ensure compliance with this subpart B.

(b) A Federal program agency must notify us if a State demonstrates an unwillingness or inability to comply with this subpart B.

(c) A Federal program agency must formulate procedural instructions specifying the methods for carrying out the responsibilities of this section.

§ 205.35 What is the result of Federal program agency or State non-compliance?

We have unilateral authority to require a State and a Federal program agency to make the affected Federal assistance programs subject to subpart A of this part, consistent with Federal assistance program purposes and regulations, notwithstanding any other provision of this part, if:

(a) A State demonstrates an unwillingness or inability to comply with this subpart B; or

(b) A Federal program agency demonstrates an unwillingness or inability to make Federal funds available to a State as needed to carry out a Federal assistance program.

Subpart C—[Reserved]

Dated: October 3, 2000.

Kenneth R. Papaj,

Acting Commissioner.

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