

WITT O'BRIEN'S

ambipar^a
response

THE SILICON VALLEY BANK (SVB) CRISIS CAUTIONARY TALE FOR GRANTEES: WHY A REIMBURSEMENT PAYMENT BASIS IS SAFER THAN ADVANCE PAYMENTS

Author

Matthew Hanson, CGMS - Associate Managing Director, Witt O'Brien's

WITH YOU
WHEN IT COUNTS

The Silicon Valley Bank (SVB) Crisis Cautionary Tale for Grantees: Why a Reimbursement Payment Basis is Safer than Advance Payments

Author:

Matthew Hanson, CGMS - Associate Managing Director, Witt O'Brien's

In the wake of the Silicon Valley Bank (SVB) crisis, your organization may not immediately see a connection between a seriously failed financial banking institution and grants financial administration/management. SVB was fraught with "too little, too late" lessons learned on diversification, and failure to raise critical capital. However, a very important lesson can be plucked from the obscurity of the SVB rubble—shedding light on an important facet of grants financial management. **Specifically, reimbursement payment structures offer a safer alternative to advance payments.**

In light of the SVB debacle, let's examine what could happen when a grantee chooses advance payments in lieu of reimbursement payments.

Sample Case Study:

Let's hypothesize "Grantee A" is the recipient of certain Federal grants funds. Grantee A issues an advance payment to a vendor because it's convenient, creating an immediate cash flow to the vendor. However, the vendor banks with a financial institution similarly situated to SVB. The financial institution collapses and goes into default on its obligations. Suddenly, the vendor does not have access to the cash flow, and the grant program is now in danger of losing money. The grant funds are therefore at risk until the Federal government steps in to mitigate the financial institution's default. However, there is something Grantee A could have done long before the collapse to put reasonable controls and safeguards in place to protect the Federal funds in this scenario. **Grantee A could have chosen to implement reimbursement-styled payments to the vendor.**

You might be asking, what is the difference between reimbursement payments and advance payments? According to Uniform Guidance 2 CFR 200.1, **Advance payment:** "means a payment that a Federal awarding agency or pass-through entity makes by any appropriate payment mechanism, including a predetermined payment schedule, before the non-Federal entity disburses the funds for program purposes."

Reimbursement payments are those payments that are rendered only after the vendor or contractor actually incurs program-related expenses and provides documentation to support said expenditures, requesting reimbursement for their fronted payment of the expense.

If your organization is administering Federal dollars as a pass-through agency, the terms and conditions of the Federal awarding agency will reflect specific conditions such as identifying preferred payment methodology or directing a pass-through entity to follow provisions such as 2 CFR 200 Uniform Guidance. The Uniform Guidance provides additional relevant guidelines in examining reimbursement payment versus advance payment options. Specifically, 2 CFR 200.305(3) states:

"Reimbursement is the preferred method when the requirements in this [paragraph \(b\)](#) cannot be met, when the Federal awarding agency sets a specific condition per [§ 200.208](#), or when the non-Federal entity requests payment by reimbursement."

Furthermore, relative to timing of payments:

"When the reimbursement method is used, the Federal awarding agency or pass-through entity must make payment within 30 calendar days after receipt of the billing, unless the Federal awarding agency or pass-through entity reasonably believes the request to be improper."^[1]

[1] *id.*



Relative to the interplay between Federal and State entities for funds transferred, under the Cash Management Improvement Act (CMIA) (as codified under 31 CFR 205), Subpart A details rules applicable to programs included in a Treasury-State agreement. Particularly, under this Subpart, certain requirements for documenting funding techniques in the agreement are detailed to wit:

"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 project 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 projection or reconciliation, is properly applied."^[2]*

For Federal assistance programs not included in a Treasury-State agreement:

*"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."^[3]*

In all three regulatory components above, we see policy which demonstrates clearly, or hedges a need for close proximity of a request for payment/actual payment of funds to the actual and immediate cash needs. In application, such payment would have to be made:

1. Within 30 days of billing receipt for entities subject to 2 CFR 200.305, or
2. Determined/outlined within a reasonable timeframe (*i.e. 3-5 business days*) under a Treasury-State agreement scenario, or
3. As soon as administratively possible for those programs not included in a Treasury-State regulation scenario.

Although advance payments may sometimes be required—or even necessary—we contend that a reimbursement payment structure is still a best practice, when possible, to protect grants funds. Further, the timeliness of payments to proximity of cash need holds program financial management to the highest accounting and documentation standards.

Reimbursement-styled payments are safer because they:

- Minimize the risk of large sums of grants money sitting/waiting for proper expenditure/justification.
- Minimize exposure of funds to scenarios such as the SVB collapse.
- Minimize Fraud, Waste and Abuse.
- Allow greater financial management/control by the pass-through/grantee over funds.
- Reduce the risk of finding non-compliant uses of funds too late in the grants cycle.
- Increase grants management efficiency because financial monitoring is ongoing with review of expenditures occurring prior to payment, rather than review of financial expenditures after payment has already occurred.

We recommend following some best practices such as:

- Regardless of whether your organization is dealing in Federal, state, or local dollars, be sure to understand and follow all award terms and conditions closely.
- Set a clear reimbursement schedule with all vendors/contractors.
- Identify and convey clear requirements around documentation of expenditures.
- Put proper internal controls in place for review of documentation, expenditures, and reimbursement requests.
- Ensure contemplation of contract terms and conditions, which may include but are not limited to: penalty structures and recoupment terms for ineligible expenditures, untimely reimbursement request submissions, improper or lacking expenditure/reimbursement documentation, and even fraud/criminal implication warnings.

[2] 31 CFR § 205.10. Available at: [eCFR :: 31 CFR Part 205 Subpart A -- Rules Applicable to Federal Assistance Programs Included in a Treasury-State Agreement](#)

[3] 31 CFR § 205.33(a). Available at: [eCFR :: 31 CFR Part 205 Subpart B -- Rules Applicable to Federal Assistance Programs Not Included in a Treasury-State Agreement](#)

