



Reviewing for Federally Defined

Allowable and Unallowable Costs

New Mexico Tech Business Office
Last modified July 21, 2015

This procedure outlines New Mexico Institute of Mining and Technology's (NMIMT) responsibilities for accounting for federally defined allowable and unallowable costs for reimbursement purposes. In addition, the procedure facilitates training of individuals involved in the coding of financial transactions, in order that they become familiar with governing regulations to ensure the proper classification of expenditures that are included in the indirect cost (overhead) rate.

This is a working document and as such, we would appreciate any information and/or insight which would help us develop stronger policies for NMIMT's research community.

Table of Contents

- I. Introduction..... 3**
- II. Definitions..... 4**
 - A. Allowability4
 - B. Cost Allocability.....4
 - C. Defense Contract Audit Agency (DCAA).....4
 - D. Direct Costs.....4
 - E. Indirect Costs.....5
 - F. Office of Naval Research (ONR)5
- III. General Information.....6**
- IV. Treatment of Unallowable Costs 8**
- V. Guidelines 9**
 - A. Determining Allowable Costs9
 - B. Defining Unallowable Costs.....9
- VI. Federally Defined Unallowable Activities 10**
 - A. General Public Relations10
 - B. Alumni Activities.....10
 - C. Defense and Prosecution in Court10
 - D. Housing and Personal Living Expenses.....11
 - E. Organized Fundraising11
 - F. Investment Management Costs.....11
 - G. Lobbying11
 - H. Selling and Marketing11
 - I. Student Activity Costs.....11
- VII. Federally Defined Unallowable Expenditures..... 12**
- VIII. Policy Authorities..... 13**
- IX. References..... 14**
- X. Flowchart 15**

I. Introduction

This procedure outlines New Mexico Institute of Mining and Technology's (NMIMT) responsibilities for accounting for federally defined allowable and unallowable costs for reimbursement purposes. In addition, the procedure facilitates training of individuals involved in the coding of financial transactions, in order that they become familiar with governing regulations to ensure the proper classification of expenditures that are included in the indirect cost (overhead) rate.

2 CFR Part 200 Office of Management and Budget's (OMB) Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards (UG) establishes principles for determining costs applicable to grants, contracts, and other agreements with educational institutions. The Uniform Guidance also provides guidelines used in preparing an overhead rate proposal. In addition, it defines **what are allowable and unallowable direct and indirect costs for federal reimbursement purposes.**

II. Definitions

A. Allowability

Allowability refers to costs, direct or indirect (F&A), that are appropriately charged to a sponsored project for reimbursement purposes. According to UG Section 200.403 and Federal Acquisitions Regulations FAR Part 31.201-2 allowable costs must meet the following general criteria in order to be allowable under federal awards:

- **Necessary and Reasonable** – The nature of goods or services acquired or applied and the amount involved reflect the action that a “prudent person” would have taken under the circumstances prevailing at the time the decision to incur the cost was made.
- **Allocable** – The process of assigning a cost or group of costs to one or more cost objectives in proportion to the benefit or other equitable relationship provided.
- **Consistently Treated** - Like expenses must be treated the same in like circumstances and uniformly applied to both federally financed and other activities and other activities of the non-federal entity.
- **Allowable** - Expenses must conform to any limitations or exclusions set forth in the UG or in the federal award as to types or amount of cost items..
- **Adequately Documented** – the foundation for supporting accounting and cost records.

B. Cost Allocability

The allocability of cost involves an assessment of the relative benefits received from the incurrence of the cost. The National Association of College and University Business Officers (NACUBO) lists three different levels of cost allocability, which are as follows:

1. Cost is incurred solely to advance work under the sponsored agreement.
2. Expense is incurred in a manner that benefits both the sponsored agreement and other work of the institution in proportions that can be approximated through the use of reasonable methods.
3. Cost is necessary for the overall operation of the institution and under the UG, deemed to be assignable in part to sponsored projects.

C. Defense Contract Audit Agency (DCAA)

The Defense Contract Audit Agency (DCAA) is a federal agency which audits NMIMT's overhead proposals on behalf of the Office of Naval Research (ONR).

D. Direct Costs

Direct costs are defined as costs that can be identified specifically with a particular sponsored project or NMIMT activity. These costs can be assigned to such activity relatively easily and

with a high degree of accuracy. Identification with the sponsored work rather than the nature of the goods and services involved is the determining factor in distinguishing direct from indirect (F & A) costs of sponsored agreements (UG Section 200.413 also refer to 200.405 Allocable Costs).

E. Indirect Costs

Indirect costs are defined as costs that are incurred for common or joint objectives and therefore cannot be identified with a particular sponsored project, an instructional activity or any other institutional activity (UG Section 200.56 and Section 200.414). Indirect costs may also be referred to as Facilities and Administrative (F&A) costs.

F. Office of Naval Research (ONR)

The Office of Naval Research (ONR) is NMIMT's cognizant federal agency. The ONR has responsibility for approving or disapproving NMIMT's proposed overhead rates.

III. General Information

The federal government provides direct support for federally sponsored agreements and reimburses NMIMT for its share of NMIMT's general operating costs (e.g., indirect or F&A costs). The government provides for the allocation of a portion of these operating costs to grants and contracts through approved indirect cost rates. Indirect cost rates are calculated and approved on an annual basis. DCAA audits both the study and proposal. The rates provided are then negotiated with the ONR.

The calculation process involves a comparison of total allocable indirect costs to modified total direct costs of a particular function. The resulting ratio is referred to as the "indirect cost rate." Indirect cost rates are calculated for the organized research function and other sponsored activities of NMIMT.

As a part of this allocation process, indirect costs are segregated into the following indirect cost pools:

Note: Refer to the appropriate section of OMB A-21 for full description of the chosen pool.

- **Building Depreciation** – compensation to NMIMT for use of buildings ((Refer to UG Appendix III to Part 200, paragraph B(2))
- **Equipment Depreciation** – compensation to NMIMT for use of equipment (Refer to UG Appendix III to Part 200, paragraph B(2))
- **Departmental Administration** – administrative and supporting services that benefit common or joint departmental activities or objectives in academic deans' offices, academic departments and divisions and organized research units. This includes the general activities performed in academic departments to support instruction and research. (Cost Category 40. Refer to UG Appendix III to Part 200, paragraph B(6))
- **General Administration and Expenses** – represents central and general executive and administrative activities of NMIMT (Cost Category 50. Refer to UG Appendix III to Part 200, paragraph B(5))
- **Sponsored Projects Administration**- departments established primarily to administer sponsored projects (*Cost Category* 60. Refer to UG Appendix III to Part 200, paragraph B(7))
- **Operations and Maintenance** – activities that have been incurred by a central service organization for the operation and maintenance of the infrastructure (*Cost Category* 80. Refer to UG Appendix III to Part 200, paragraph B(4))
- **Library** – activities that directly support the operation of the library (*Cost Category* 70. Refer to UG Appendix III to Part 200, paragraph B(8))

The activities in the accounts assigned to these pools must be consistent with the UG's definition of the function and must not include expressly unallowable costs outlined under *UG* Section 200.420

NMIMT is legally required to submit a certification with each indirect cost rate proposal attesting to the fact that no unallowable expenses are included in the indirect cost rate proposal. Sanctions for non-compliance include non-recovery of indirect costs and penalties of perjury for false certification. Federal regulations stipulate that all indirect costs deemed unallowable by the government are subject to a penalty equal to the amount of the disallowed expense plus interest.

IV. Treatment of Unallowable Costs

The term unallowable cost does not mean that the charge is unlawful, improper, or even wrong. In the context of cost recovery as defined in the UG, it means that the federal government will not participate either directly or indirectly in the cost.

For F&A preparation purposes, NMIMT handles unallowable costs (for federal reimbursement purposes) in the following manner:

- A. In each allocation base: Unallowable costs are not removed from the MTDC base of Instruction, Research or Other Institute Activities (OIA) and hence receive a full allocation of indirect costs.
- B. In each indirect expense pool: Unallowable costs are removed before the allocation to cost objectives. Costs coded as unallowable are transferred to Other Institute Activities which then becomes part of the OIA base/denominator and accordingly the unallowable costs bear their share of F&A.
- C. Service Centers: Unallowable costs are removed from service center costs when developing rates and charged to discretionary funds. Discretionary funds can be generated from the difference between direct cost recovery and market rates charged to External Users. The discretionary FUNDS are coded as part of the OIA allocation base and accordingly the unallowable costs bear their share of F&A. For more detail on the subject see the [Service Center Procedure Manual](#).

V. Guidelines

A. Determining Allowable Costs

The UG's tests of expenditure allowability states that costs must meet the following criteria

- **Necessary and Reasonable** – The nature of goods or services acquired or applied and the amount involved reflect the action that a “prudent person” would have taken under the circumstances prevailing at the time the decision to incur the cost was made.
- **Allocable** – The process of assigning a cost or group of costs to one or more cost objectives in proportion to the benefit or other equitable relationship provided.
- **Consistently Treated** - Like expenses must be treated the same in like circumstances and uniformly applied to both federally financed and other activities and other activities of the non-federal entity.
- **Allowable** – Expense must conform to any limitations or exclusions set forth in the UG or in the federal award as to types or amount of cost items.
- **Adequately Documented** – the foundation for supporting accounting and cost records.

Note: If an expense cannot meet the above criteria, it is not eligible for inclusion in the indirect cost rate study regardless of its purpose.

Agencies that sponsor grants and contracts use the term allowable to mean “permitted as a direct cost under the terms of a specific grant or contract.” Expenses that are generally allowable for federal reimbursement may not necessarily be permitted under the terms of a specific grant or contract. Review the terms of the agreement in order to determine the appropriateness of charge.

B. Defining Unallowable Costs

Costs are specifically unallowable under two general conditions:

1. The costs are for an unallowable **activity** (something you do and record using a FUND).
2. The costs are for an unallowable **expenditure** (something you buy, a line item recorded at the account code level).

NMIMT tracks whether activities are allowable for reimbursement through the FUND number to which transactions are charged and tracks allowable and unallowable transactions at the expenditure account code level. Therefore, it is imperative to understand the definition of the cost category that has been assigned to the Fund number(s) used.

If you find yourself engaged in activities that deviate from the intended purposes of your FUND, you must bring it to the attention of either the Director of Sponsored Projects or Cost Accounting Manager. If you are incurring an unallowable expense in an otherwise allowable FUND, you must code the transaction with an Account code 730000 or higher.

VI. Federally Defined Unallowable Activities

Unallowable Activities are generally recorded in separate FUNDS specifically designated for these purposes. Allowable account codes may be used with these FUNDS since the FUND is not incorporated into the overhead study for reimbursement purposes. These activities may be appropriate and permissible NMIMT type functions; however, the federal government will not reimburse NMIMT for these costs.

The Uniform Guidance Section 200.420 describes fifty-five selected types of cost items, some of which are unallowable for reimbursement purposes. In reviewing costs in each of these areas, please keep in mind that the federal government identifies "associated costs" with unallowable costs. In case of a conflict between provisions in the UG and the provisions of a specific agreement, the terms of the specific agreement govern.

Note: The following list is not meant to be all-inclusive.

A. General Public Relations

General Public Relations include community relations and activities dedicated to maintaining the image of the institution or promoting understanding and favorable relations with the community (UG Section 200.421 paragraph (d)).

The only allowable public relations costs are:

- Costs specifically required by sponsored agreements.
- Costs of communicating with the public and press pertaining to specific activities or accomplishments which result from performance of sponsored agreements.
- Costs of conducting general liaison with news media and government public relations officers, to the extent that such activities are limited to communication and liaison necessary to keep the public informed on matters of public concern (e.g., notices of contract/grant awards, financial matters, etc.).

B. Alumni Activities

Costs incurred for, or in support of, alumni and similar activities are unallowable (UG Section 200.424).

C. Defense and Prosecution in Court

Defense and prosecution of criminal proceedings, civil proceedings, claims, appeals, and patent infringement are considered unallowable (UG Section 200.435).

D. Goods or services for personal use

Costs of housing, (e.g., depreciation, maintenance, utilities, furnishings, rent, etc.), housing allowances, and personal living expenses are only allowable as direct costs regardless of whether reported as taxable income to the employees. In addition, to be allowable direct costs must be approved in advance by a Federal awarding agency (UG Section 200.445 (b)).

E. Organized Fundraising

Costs of organized fundraising including financial campaigns, endowment drives, solicitation of gifts and bequests, and similar expenses incurred solely to raise capital or obtain contributions are unallowable (UG Section 200.442).

F. Investment Management Costs

Costs of investment counsel/staff and similar expenses incurred solely to enhance income from investments are unallowable except when associated with investments covering pension, self-insurance or other funds which include Federal participation allowed by this part.(UG Section 200.442 (b)).

G. Lobbying

Attempts to influence the outcomes of any federal, state or local election, referendum, initiative, or similar procedure through monetary contributions, endorsements, publicity or similar activity are unallowable. (UG Section 200.450 (c)(1)(i)).

H. Selling and Marketing

The UG Section 200.467 states that costs of selling and marketing any products or services of the institution (unless allowed under Section 200.421 Advertising and public relations) are unallowable except as direct costs, with prior approval by the Federal awarding agency when necessary for the performance of the Federal award.. This activity differs from bid and proposal development costs (UG Section 200.460) in that marketing is defined as the unsolicited promotion of NMIMT. Bid and proposal work is when an outside entity contacts you to develop a proposal.

I. Student Activity Costs

Costs incurred for intramural activities, student publications, student clubs, and other student activities are unallowable, unless specifically provided for in the Federal award.(UG Section 200.469).

VII. Federally Defined Unallowable Expenditures

In addition to unallowable activities, certain costs are always unallowable, regardless of the activity they support. These costs are unallowable by expenditure type and are typically recorded in s p e c i f i c general ledger expense account codes designed to segregate these costs from allowable costs.

- **Advertising and Public Relation** – Costs designed solely to promote the institution (Section 200.421(e)(4)).
- **Alcoholic Beverages** – (UG Section 200.423).
- **Certain Recruitment Costs** – relocation costs when newly hired employee resigns within 12 months of hire (Section 200.463(c)).
- **Certain Travel Costs** – Costs such as first-class travel (Section 200.474 (d)).
- **Entertainment** – Refer to Section 200.438).
- **Fines and Penalties** – Section 200.441.
- **Goods and Services for Employee’s Personal Use** – Section 200.445.
- **Losses on Other Sponsored Agreements** – Section 200.451.
Memberships in Civic, Community, or Social Organizations – Includes country club or social or dining club are unallowable (Section 200.454).
- **Memorabilia and Promotional Materials** – Section 200.421(e)(3).

In many cases, determining the allowability or unallowability of a particular cost is complex. When in doubt, consult with the Director of Finance, Director of Sponsored Projects, Controller or Cost Accounting Manager.

VIII. Policy Authorities

The policy authorities are the Director of Finance and the Vice President of Administration and Finance.

IX. References

Code of Federal Regulations Title 2: Grants and Agreements Part 200 Uniform Administrative Requirements, Cost Principles and Audit Requirements for Federal Awards.

Federal Acquisition Regulations, FAR Part 31.201-2 Determining Allowability

Cost Accounting Standard (CAS) 9905-505, "Accounting for Unallowable Costs - Educational Institutions."

Council on Governmental Relations (COGR). *Managing Externally Funded Programs at Colleges and Universities: A Guideline to Good Management Practices*. November 2001.

National Association of College and University Business Offices (NACUBO). *A Guide to Managing Federal Grants for Colleges and Universities*.

National Council of University Research Administrators (NCURA). *Regulation and Compliance*. 2004 Edition

X. Flowchart

