

Guide 1305 GD.07

Determining Allowability, Reasonableness, and Allocability of Costs for Sponsored Projects

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Overview

When a sponsor awards funds to the University in support of specific programs and projects, it requires the University to manage those funds prudently to ensure that any costs incurred directly benefit the project accounts being charged.

- The Federal Government is the largest sponsor of externally funded activity at the University. The cost principles relating to expenditures on federal awards are contained in the Office of Management and Budget's (OMB) [Circular A-21](#) *The Cost Principles for Institutions of Higher Education*. These cost principles require that any expense charged to a federally sponsored project be reasonable and necessary, allocable, consistently treated, and conform to any limits or exclusions set forth in A-21 or the terms and conditions of the award.

In addition, individual awards may include special terms and conditions which must be considered when incurring costs. Consult with the appropriate Grant and Contract Administration (GCA) office for more details.

The University is committed to ensuring that all cost transfers (either in the form of a labor distribution adjustment or non-salary journal entry) are appropriate and are conducted in accordance with sponsor terms and conditions, regulations, and University policy ([Policy 1305](#) Cost Transfers Involving Sponsored Projects). Grant and Contract Financial Administration (GCFA) has the authority to approve/disapprove cost transfers. Cost transfers found later to be inappropriate will be reversed and charged to an appropriate source within the department.

Allowable Costs

All costs must be allowable under federal regulations and sponsor terms and conditions, including program-specific requirements and University policy. To be allowable, costs must:

- be reasonable and necessary;
- be allocable to federally sponsored projects under the principles and methods provided in OMB Circular A-21;
- be given consistent treatment; and
- conform to any limits or exclusions set forth in A-21 or the terms and conditions of the award.

OMB [Circular A-21](#) spells out in great detail the allowability of particular elements of cost. When an item is questionable, GCA or GCFA should be consulted **before** the cost is incurred.

Typical costs charged directly to a sponsored project include:

- compensation of employees for performance of work under the sponsored agreement, including related fringe benefit costs;
- costs of materials consumed or expended in the performance of the sponsored project;
- travel in accordance with the University's policy ([Policy 3301](#) Travel on University Business);
- other allowable items of expense incurred for the sponsored project.

Costs of materials from stock/services rendered by specialized facilities or other institutional service operations may be included as costs under federally sponsored agreements, provided such items are:

- consistently treated in similar circumstances as direct costs, rather than Facilities and Administrative (indirect) costs; and
- charged under a recognized method of computing actual costs.

Reasonable Costs

OMB Circular A-21 defines a cost as reasonable if the nature of the goods or services acquired or applied, and the amount involved, reflect the action that a *prudent person* would have taken under the prevailing circumstances when the decision to incur the cost was made.

Important considerations in determining the reasonableness of costs are:

1. Is the cost of a type generally recognized as necessary for the operation of the institution or the performance of the sponsored project?
2. Have the restraints or requirements imposed by such factors as federal and state laws and regulations, sponsored agreement terms and conditions, and arm's-length bargaining been satisfied?
3. Have the individuals concerned acted with due prudence in the circumstances, considering their responsibilities to the institution, its employees, its students, the government, and the public at large?
4. Is the extent of the actions taken with respect to the incurrence of the costs (e.g., hiring decision, choice of goods or services, determination of salary or price, vendor selection, etc.) consistent with established institutional policies and practices applicable to the work of the institution generally, including sponsored projects?

Allocable Costs

A cost is allocable to a particular cost objective (i.e., a specific function, project, sponsored agreement, department, or the like) if the goods or services involved are chargeable or assignable to such cost objective in accordance with relative benefits received or other equitable relationship. Every incurred cost must have a direct benefit to the sponsored project being charged.

In general, a cost is allocable to a particular sponsored project if it fulfills one of the following conditions:

- it is incurred solely to advance the work under the sponsored agreement; or
- it benefits both the sponsored agreement and other work of the institution, in proportions that can be approximated through use of reasonable methods; or
- it is necessary to the overall operation of the institution and, in light of the principles provided in OMB Circular A-21, is deemed to be assignable in part to sponsored projects.

If a cost benefits two or more projects or activities in proportions that can be determined without undue effort or cost, the cost should be allocated to the projects based on the proportional benefit. If a cost benefits two or more projects or activities in proportions that cannot be determined because of the interrelationship of the work involved, then the costs may be allocated or transferred to benefited projects on any reasonable basis.

Note: Reasonable methods of allocating common use scientific items and supplies may include proportional benefit, specific anticipated use per award, FTEs on each award, lab square footage, high correlation to another lab cost that is clearly allocated, and MTDC proportions (i.e., relative size of non-salary budget, excluding equipment, tuition, and any subcontracts).

In the rare instances in which a proper cost allocation cannot ultimately be determined using any reasonable methods, the cost may be charged to a single sponsored project.

Where the purchase of equipment or other capital items is specifically authorized under a sponsored agreement, the amounts thus authorized for such purchases are assignable to the sponsored agreement regardless of the use that may subsequently be made of the equipment or other capital items involved.

Any costs allocable to a particular sponsored agreement under the standards provided in OMB Circular A-21 may not be shifted to other sponsored agreements in order to meet deficiencies caused by overruns or other fund considerations, to avoid restrictions imposed by law or by terms of the sponsored agreement, or for other reasons of convenience.

Any costs allocable to activities sponsored by industry, foreign governments, or other sponsors may not be shifted to federally sponsored agreements.