

Guidelines for Cost Categorization in Nonprofit Contracts and Grants

Version 2.0 – July 16, 2025

SUMMARY

In Version 2.0, the Controller's Office updated the Guidelines for Cost Categorization in Nonprofit Contracts and Grants in accordance with the federal Office of Management and Budget's October 2024 revisions to the Uniform Guidance. The Controller's Office expanded upon guidance for direct and indirect costs, including net wages, fringe benefits, de minimis rates, and more.

BACKGROUND

In 2010, the Controller's Office issued a memo in response to City department and nonprofit inquiries concerning nonprofit indirect cost rates. After analysis of federal guidelines, best practices, and discussions with City departments, the Controller's Office issued a memo including, among others, the finding that no single list can encompass the full extent of charges that may fall under an indirect cost category.

In subsequent years, there have been advancements in standardizing policies and procedures, most notably the federal Office of Management and Budget (OMB) Uniform Guidance published in 2014.

The OMB revised the Uniform Guidance – a component of the Guidance for Federal Financial Assistance, formerly the Guidance for Grants and Agreements – in October 2024. The updates incorporate statutory requirements and administration priorities, reduce agency and recipient burden, clarify sections that recipients or agencies interpreted in different ways, and rewrite applicable sections in plain language to improve flow and address inconsistent use of terms.

The Controller's Office created this document in alignment with the Guidance for Federal Financial Assistance to assist City departments in determining allowable and unallowable contract costs, as well as distinctions between direct and indirect costs in nonprofit contracts.

"There is no universal rule for classifying certain costs as direct or indirect costs. A cost may be direct for some specific service or function but indirect for the Federal award or other final cost objective. Therefore, each cost incurred for the same purpose in like circumstances must be treated consistently either as a direct or an indirect cost to avoid possible double-charging of Federal awards."

OMB Uniform Guidance Part 200 Sec. 200.412 Classification of Costs.

This update supersedes the version the Controller's Offices issued in January 2019. The Controller's Office may make periodic updates to these guidelines as needed.

GUIDELINES

The Controller's Office developed this consolidated set of budget guidelines to foster common understanding and transparency on the treatment and allowability of direct and indirect costs in nonprofit

contracts. This document provides guidance that addresses the most common costs, though it is **not inclusive of all possible costs or their treatment**. Some discretion may be necessary as departments and nonprofit contractors develop contract budgets based on programmatic needs.

The guidelines serve as a starting point as City staff and nonprofits collaborate to ensure all parties have a shared understanding of budgeting principles, allowability of costs, and the application of these guidelines. Further guidance on nonprofit financial management practices (including cost allocation principles) can be found in the Controller's Office's [Finance Guide for Nonprofits](#).

Key Principles for Cost Allowability

In accordance with federal standards per the OMB, these guidelines indicate which direct and indirect costs are **allowable** to include within City contracts and grants, whether they may be explicitly allowable as a direct or indirect expense, and which types of costs are explicitly unallowable across all City contracts.

In the course of contracting, City departments determine which allowable costs align to the objectives of the contract, and these are considered **approved costs** (also called "**eligible costs**"). Departments may prioritize certain expenditures over others during contract negotiations and may not approve some "allowable" costs in a given contract. For example, while rent is "allowable" for City contracts generally, a contract may or may not include rent as an approved use of contract funds based on the objectives for that contract.

- Departments should clearly state which cost categories are approved or not approved within each contract (e.g., within G100 Appendix A: Eligible Costs), and the contract budget should align.
- **Departments must only approve costs in contracts that align to the terms of the funding source.** These guidelines provide general principles for allowability. However, federal or state grants may have specific terms that differ from these guidelines. For example, a federal grant may only allow funding for salaries, or may not allow funding for rent costs, etc. Departments must always defer to the specific allowability of a funding source where it may differ from these guidelines.
 - When a funding source deems certain costs unallowable (e.g., if a federal grant does not allow funds to be used on stipends, food, etc.), departments should **include a list of such expenses as ineligible within the contract** (e.g., within G100 Appendix A: Eligible Costs).
- Departments may require **supplemental approval processes** for some expenses prior to considering these eligible within the contract or grant budget, e.g., for travel and training costs, capital or equipment, and/or subcontractors, among others. When supplemental approval is needed, departments should inform contractors of the process during contract negotiations and should confirm in writing when any such supplemental approvals have been granted.
- All expenditures must be **reasonable, necessary, and directly aligned** with the stated purpose of the contract or grant. Any costs deemed excessive, inconsistent with the contract's objectives, or not representing a prudent use of public funds will be considered ineligible.
- **Shared costs must be allocated appropriately to be deemed allowable.** Shared costs are those that are necessary to all program operations, but not specific to a single program. This may include rent (when a facility is used for more than a single program), equipment shared across programs, IT

and materials shared across programs, etc. Shared costs must be allocated proportionally across program and administrative cost centers using a consistent and reasonable methodology.

- **Contractors must maintain accurate financial books and accounting records** relating to eligible expenses incurred and funds received and expended under each City agreement. This includes invoices, receipts, payroll records, time records, canceled checks or bank records showing proof of payment and/or other financial records for costs funded in whole or in part by the City.

As a best practice, departments should establish clear contract-related budgeting policies to specify any costs that will be unapproved or ineligible across all contracts or specific types of contracts, as well as any supplemental approvals that may be needed for certain costs to be included and approved within a contract.

CHANGES FROM PRIOR VERSION

The Controller's Office will periodically update this document as departments and nonprofits raise new questions about the guidance. Version 2.0 replaces Version 1.2 published in 2019. This section outlines changes incorporated based on department inquiries and/or updates to the Uniform Guidance.

Cost Categorization Updates

See the Cost Categorization Guidance section of this document for more details on the following changes:

- **Worker's compensation** added as allowable Fringe Benefits.
- **Legal holidays** added as allowable Fringe Benefits.
- Salary and Fringe costs for administrative staff, like an Executive Director, added as allowable when these staff work on direct program activities/services and costs have been appropriately allocated.
- **Paid Sabbaticals** added as unallowable costs.
- Clarifications for when and how **accrued leave time and/or vacation payouts** may be allowable.
- **Staff incentives** that are not for direct program purposes added as unallowable costs.
- **Credit card fees** added as unallowable costs.
- **Subcontract** costs updated to include subcontracts of a subcontractor as allowable.

Supplemental Guidance Updates

See the Supplemental Guidance section of this document for more details on the following changes:

- **Salaries/Fringe Benefits:** Definition of "net wages" as a term frequently used in contracts.
- **De Minimis Rate:** OMB raised the de minimis rate from 10% to 15%.
- **Subcontractor Costs:** OMB raised the threshold for how much of a subcontractor's costs a prime contractor may charge indirect costs for, from \$25,000 to \$50,000.

Cost Categorization Guidance

Direct Costs

Direct program expenses must be approved by the funding department and documented in the grant or contract budget. While costs may be allowable, allowability does not guarantee funding in a particular cost category. Departments and nonprofits should negotiate appropriate and reasonable funding for cost items aligned to the delivery of contracted programming and funding source guidelines. Departments may require additional documentation prior to approving certain costs and may set a cap on the amount of funding available for certain costs based on funding priorities.

Category	Expense Type	Expense Description	Allowable	Unallowable	Notes
Direct Personnel Expenses	Salaries	Salaries of all program staff, supervisory staff, and support/clerical staff that work directly on programs.	x		If administrative staff, like an Executive Director, work on direct program activities/services, then the corresponding percentage of that staff's time may be allocated as a direct expense.
		Paid leave, including legal holidays, administrative leave and sick time.	x		Paid leave costs may appear in organizational budgets as either fringe benefits or salaries.
		Bonuses paid to staff.		x	
		Severance payments to former staff.		x	
	Fringe Benefits	Fringe Benefits such as FICA, SUI, health and medical benefits, retirement benefits and/or worker's compensation.	x		
		Prior fiscal year Fringe Benefits such as vacation, sick, or overtime/compensation time, and taxes or other withholdings related to periods before and after the grant agreement.	x*	x**	* If a nonprofit uses a cash basis, the cost of leave is recognized in the period that the leave is taken and paid for, even if earned in the prior year, and this cost is allowable.

Category	Expense Type	Expense Description	Allowable	Unallowable	Notes
Direct Contract Expenses					** Unallowable when a nonprofit uses an accrual basis for accounting (recommended).
		Lump sum payout of unused vacation or compensatory time		x	If a nonprofit uses a cash basis, payouts for unused leave are allowable as an <u>indirect</u> cost in the year of payment, but not allowable as a direct cost. When a nonprofit uses accrual-based accounting, the City has already covered the cost of fringe, which then becomes a line in the nonprofit's liability account.
	Contractual Services	Contractual Services provided to program participants or nonprofit by consultants, independent contractors, or other entities that are non-staff individuals.	x		Contractual Services may require supplemental approval prior to placing costs into the grant budget and the contractor must comply with City standards for subcontract oversight and monitoring.
Direct Non-Personnel Expenses	Materials and Supplies	Materials and supplies used in the operation of the program and consistent with the type of services provided by the program. Includes project supplies, office supplies, and postage.	x		
	Stipends	Stipends, including small amounts paid to someone (often a program participant) for engaging in limited periods of work in support of a funded agency or organization.	x		Departments should consult with the Office of Labor Standards Enforcement (OLSE) to determine when a program stipend must be treated as a salary.

Category	Expense Type	Expense Description	Allowable	Unallowable	Notes
	Facilities/ Occupancy	Facilities or occupancy costs associated with building space, rental/lease of space used to run the program, rent for main space and auxiliary space, and costs associated with facility upkeep and maintenance, including janitorial services.	x		Should the City mandate capital upgrades, departments have discretion to approve relocation rental costs during renovation.
		Facilities or occupancy costs such as property taxes, loans against own property, and security deposits.		x	
	Utilities	Percentage allocation of utilities, such as gas, electric, and water bill, used by each program.	x		
	Equipment	Equipment purchase, lease, and maintenance costs that directly benefit program participants. Includes computers, IT systems, furniture, ongoing or one-time lease, printers, and photocopying equipment. Includes direct costs or percentage allocation of shared equipment used by each program.	x		
	Transportation/ Travel	Transportation and travel costs used for the program. Includes local transportation, out-of-town travel for program purposes, and field work. Includes mileage, vehicle rental, tolls, gas, parking costs, air travel, and ground transportation if staff are required to travel to perform scope of funded services.	x		Departments may require supplemental approvals for air travel, out of state travel, vehicle rental, or other specific travel costs.
		Vehicle purchase (and related costs) as required to perform scope of funded services.	x		Most departments require pre-approval prior to placing vehicle purchase into the contract budget.

Category	Expense Type	Expense Description	Allowable	Unallowable	Notes
					The contract should define asset disposition guidelines and the treatment of expenditures once the contract is complete and when the asset (vehicle) is not fully depreciated. Following federal rules for equipment, the contractor should be reimbursed either by depreciation amounts for the duration of the contract or assessing for market value at the end of the contract term and adjusting if above a certain threshold.
		Parking/moving violation fines.		x	
	Training	Staff development costs used to pay registration or attendance fees for staff to attend workshops or trainings aimed to build capacity for the program. Staff development costs may include out-of-town conferences, including transportation, lodging, food or per diem for staff.	x		
	Events and Food	Events and field trip costs related to the program. Includes vehicle rentals for participants, transportation for participants, food/meals for participants, and costs of permits needed for events.	x		
		Alcoholic beverages, sugar-sweetened beverages, and/or bottled water.		x	
		Tips/gratuity	x		Tips may also be associated with other allowable direct program

Category	Expense Type	Expense Description	Allowable	Unallowable	Notes
					costs. Per the Controller's Accounting Policies and Procedures Section 4.7.3, "For tips not covered by the GSA incidentals per diem, the amount should generally be 15%."
	Program Incentives	Incentives for program participants. Includes gift cards, honoraria, and awards for participants, speakers, and volunteers.	x		
	Insurance	Insurance fees for required insurance policy maintenance costs such as commercial general liability, auto, workers compensation, and event insurance. Includes direct allocation of program-specific policies or percentage allocation of applicable agency-wide insurance costs.	x		
	Tele-communications	Telecommunications costs used for the program. Includes telephone, fax, internet, and cell phones used for programmatic purposes.	x		
	Capital and Mortgage	Capital costs for real property necessary for the delivery of programs.	x		See Supplemental Guidance for details. Certain federal funding sources may restrict use of funding on these costs.
		Mortgage Principal.		x	See Supplemental Guidance for details.
		Mortgage interest fees on real property used in the delivery of programs.	x		See Supplemental Guidance for details. Certain federal funding sources may restrict use of funding on these costs.

Category	Expense Type	Expense Description	Allowable	Unallowable	Notes
		Mortgage interest attributable to fully depreciated assets.		x	
	Miscellaneous	Professional licenses for staff, if required for program.	x		
		Job posting and finger-printing of program staff, if required for program.	x		

Indirect Costs

Indirect costs are those that have been incurred for common or joint objectives and cannot be readily identified with a particular final cost objective.¹ Simply stated, they are organizational costs that cannot be isolated to an individual program or contract. At departmental discretion, indirect costs may be capped. If an agency has a federally-approved indirect cost rate, departments must use this rate for federally-funded contracts or grants but are not required to use that rate in General Fund contracts or grants.

Category	Expense Type	Expense Description	Allowable	Unallowable	Notes
Indirect Personnel Expenses	Salaries	Direct or percentage allocation of Executive Director salary and benefits for time spent in administrative activities (e.g., per functional time sheet or time survey).	x		If administrative staff, like an Executive Director, work on direct program activities, then the corresponding percentage of that staff's time may be allocated as a direct expense. This portion must be prorated from the percentage allocation applied to indirect costs and timesheets will be necessary to document the allocation.
		Chief financial officer salary.	x		
		Contract administration and compliance staff salaries.	x		If a contractor's cost for contract compliance activities (e.g., program monitoring and reporting) can be directly tied to a specific program (e.g., through a time study), the allocated portion of these costs may be allowable as direct expenses in a contract budget. General contract administration and compliance costs that cannot be tied to a specific

¹ Office of Management and Budget. (2004, May 10). Circular A-122. Retrieved from https://www.whitehouse.gov/sites/whitehouse.gov/files/omb/circulars/A122/a122_2004.pdf.

Category	Expense Type	Expense Description	Allowable	Unallowable	Notes
					program must be treated as an indirect cost.
		Other administrative staff salaries, including accounting, bookkeeping, human resources, information technology staff, etc.	x		
		Staff time spent preparing proposals for federal or non-federal grants and contracts.	x		
		Paid leave, including legal holidays, administrative leave and sick time, for administrative staff as listed in this section.			Paid leave costs may appear in organizational budgets as either fringe benefits or salaries.
	Fringe Benefits	Fringe Benefits such as FICA, SUI, health and medical benefits, retirement benefits and/or worker's compensation for administrative staff as listed in this section.	x		Departments may establish policies to cap approved fringe benefits in contracts.
		Lump sum payout of unused vacation or compensatory time for administrative staff as listed in this section.	x*	x**	*If a nonprofit uses a cash basis, payouts of unused leave for direct program staff are allowable as an indirect cost in the year of payment. **This is an unallowable cost if the nonprofit uses an accrual basis for accounting.
		Paid Sabbatical.		x	Sabbaticals may only be used within institutes for higher education and may only be used for graduate education or research related to the grant's program. They may not be used as a retention or incentive strategy outside institutes for higher education.

Category	Expense Type	Expense Description	Allowable	Unallowable	Notes
Indirect Contract Expenses	Contractual Services	Audit fee.	x		
		Fiscal sponsor or fiscal agent fee.	x		
		Payroll fees and other HR expenses.	x		
		Accounting services and bookkeeping.	x		
		Administrative IT system costs (e.g., QuickBooks).	x		
		Website design, maintenance, or hosting services.	x		
		Legal services.		x	Any services to be provided by a law firm or attorney must be reviewed and approved in writing in advance by the City Attorney. No invoices for services provided by law firms or attorneys, including, without limitation, as subcontractors of Contractor, will be paid unless the provider received advance written approval from the City Attorney.
Indirect Non-Personnel Expenses	Materials and Supplies	Office supplies or percentage allocation of office supplies used by administrative staff.	x		
		Materials and supplies associated with board meetings.	x		
	Facilities/Utilities	Percentage allocation of rent and utilities used by administrative staff.	x		
		Depreciation on real property	x		See Supplemental Guidance for details.

Category	Expense Type	Expense Description	Allowable	Unallowable	Notes
	Equipment	Percentage allocation of equipment used by administrative staff.	x		
		Depreciation on purchased equipment.	x		See Supplemental Guidance for details.
	Transportation/Travel	Transportation expenses incurred by administrative staff.	x		
	Insurance	Percentage allocation of insurance fees for required insurance policy maintenance costs such as commercial general liability, auto, workers compensation, and event insurance.	x		
		Directors and Officers insurance fees.	x		
	Training	Staff development costs used to pay registration or attendance fees for staff to attend workshops or trainings aimed to build capacity for the agency overall (e.g., attended by finance or HR staff).	x		
	Events and Food	Entertainment, including social activities, events or field trips that only benefit staff members, such as staff recognitions, celebrations, events attended by staff only, food for staff, and staff meals at restaurants, and related tips/gratuity.		x	
		Agency-wide events, including food purchases, without specific program benefit but in support of the agency overall (e.g., programs open house, program planning retreat).	x		

Category	Expense Type	Expense Description	Allowable	Unallowable	Notes
		Tips/gratuities for agency-wide events without specific program benefit (e.g., programs open house).	x		Tips may also be associated with other allowable indirect costs. Per the Controller's Policies and Procedures Section 4.7.3, "For tips not covered by the GSA incidentals per diem, the amount should generally be 15%."
		Alcoholic beverages, sugar-sweetened beverages, bottled water.		x	
	Tele-communications	Percentage allocation of telecommunications costs for administrative staff.	x		
	Miscellaneous	Nominal bank charges such as those required for maintaining a checking account.	x		
		Bank fees such as interest, late/penalty fees, non-sufficient service fee/overdraft fees, cash advance fee, foreign exchange fees, and credit card fees.		x	
		Credit card fees.		x	
		Staff incentives such as paid parking spots, technology or commuting stipends, and/or bonuses.		x	Staff incentives (benefits that are not directly related to program activities) are unallowable. Contractors might also incorporate incentives into a fringe benefit calculation. These costs are unallowable and departments should verify incentives are deducted from fringe calculations during contract negotiations.

Category	Expense Type	Expense Description	Allowable	Unallowable	Notes
		Personal costs.		x	
		Religious workshops, instruction or proselytization.		x	
		Bad debts including losses and related collection and legal costs.		x	
		Political activities.		x	

Fundraising Costs

Fundraising expenses are never allowable in City contracts or grants unless the program objective for the City contract or grant is defined as fundraising and/or development capacity building. Departments may offer contracts or grants specific to supporting or enhancing nonprofit capacity for fundraising and in these cases any of the following costs may be allowable as direct program costs. When the program objective is not specific to fundraising activities, fundraising expenses are unallowable per federal guidelines.

Category	Expense Type	Expense Description	Allowable	Unallowable	Notes
Fundraising Expenses	Salaries/ Fringe Benefits	Development Director or other staff with fundraising as a primary job role.		x	
		Direct or percentage allocation of Executive Director salary and benefits for time spent in fundraising activities (e.g., per functional time sheet or time survey).		x	
	Contractual Services	Fundraising consultant fees.		x	
	Materials and Supplies	Office supplies (including postage) or percentage allocation of office supplies used by fundraising staff.		x	
	Facilities/Utilities	Percentage allocation of rent and utilities used by fundraising staff.		x	
		Space rental for fundraising events.		x	
	Equipment	Percentage allocation of equipment used by fundraising staff.		x	
	Transportation/ Travel	Transportation expenses incurred by fundraising staff.		x	
	Insurance	Percentage allocation of insurance fees for required insurance policy maintenance costs such as commercial general liability, auto, workers compensation, and event insurance.		x	

Category	Expense Type	Expense Description	Allowable	Unallowable	Notes
	Training	Staff development costs used to pay registration or attendance fees for staff to attend workshops or trainings aimed to build capacity for fundraising.		x	
	Events	Fundraising event costs.		x	
	Tele-communications	Percentage allocation of telecommunications costs for fundraising staff.		x	

Supplemental Guidance

For full text of the Office of Management and Budget (OMB) Federal Financial Assistance, visit: <https://www.federalregister.gov/documents/2024/04/22/2024-07496/guidance-for-federal-financial-assistance>.

Salaries and Fringe Benefits

The current G-100 template for grant agreements provides an example of eligible costs as “net wages,” but does not define this term in the template. Per the payroll service ADP, “net wage” refers to the difference between the employee’s hourly wage minus a variety of deductions, some of which may be voluntary and others mandatory, resulting in the employee’s take home pay.²

Such deductions may include FICA, SUI, health and medical benefits, retirement benefits and/or worker’s compensation. Mandatory and voluntary deductions may be included as part of a “fringe benefits” line item.

While gross wages and certain fringe benefits are generally allowable costs in City contracts, when a contract is structured such that fringe benefits are captured as a rate that covers the cost of various mandatory and voluntary deductions, then only the portion of salaries net of these deductions may be included in the salary line item of the contract.

When negotiating contracts, departments should understand how the contractor establishes a fringe benefit rate, which deductions to the salary may be included in that rate, and what other benefits may be added to that rate. Departments should ensure that salary costs included in the contract are net of any deductions captured within the fringe benefit rate. As part of this review, departments should also ensure that fringe benefits do not include other staff incentives that are not allowable, such as gym membership stipends, etc.

Reference: OMB Uniform Guidance Part 200 Section 200.430-200.431 Compensation – Personal Services & Fringe Benefits.

Subcontracts

Subcontracted services are allowable as direct costs when necessary to support the final cost objective of the contract. As such, these direct costs may be used in the calculation of the prime contractor’s indirect cost rate with some limitations. The prime contractor can charge indirect costs on the first \$50,000 of each subcontract at the approved indirect cost rate. Additional subcontract expenses beyond \$50,000 must be excluded from the indirect rate calculation.

Subcontractors³ may include:

- Consultants: firms providing a consulting service as part of the program objective, such as an evaluator of a new initiative.

² “Gross pay vs. net pay: What’s the difference?” ADP. Accessed March 4, 2025. <https://www.adp.com/resources/articles-and-insights/articles/g/gross-pay-vs-net-pay.aspx>.

³ This does not refer to subcontracts for goods, such as equipment purchases.

- Service Partner: other nonprofits subcontracted to provide a portion of the services in the contract, which may include providing direct client services.
- Professional Service Provider: a firm hired to perform a service for the prime contractor, such as a filmmaker hired to record a cultural event.

This federal requirement limits the amount a prime contractor may claim in its own indirect costs for services the prime contractor will not perform itself. Prime contractors should establish agreements with subcontractors that specify the terms of the subcontract agreement and payment schedule, and subcontractors may propose subcontract fees that include allocated administrative costs and shared costs for the direct services provided through the subcontract. A subcontractor's allocated costs are not impacted by the OMB's cap on the prime contractor's indirect rate associated with these costs.

Should contractors seek to hire subcontractors, they must refer to the contract to ensure allowability, and in most cases, departments require pre-approval prior to using contract funds on subcontractor costs. All subcontractor costs must be approved in the contract budget. Departments may use Appendix E of the G-100 template or as approved by the City Attorney's Office, may use a supplemental process to document and approve subcontractors.

Reference: OMB Uniform Guidance Part 200 Section 200.1 Definitions - Modified Total Direct Cost (MTDC)

Indirect Rates and De Minimis Rates

Indirect rates and de minimis rates are cost reimbursement thresholds departments pre-set or negotiate with contractors. Typically, indirect rates pay for administrative costs necessary to execute a program. "De minimis rate" is the term the federal government uses to refer to a baseline allocation for indirect costs that does not require negotiation or cost allocation documents. Nonprofits may negotiate with the federal government to establish an indirect rate above the de minimis rate. The OMB raised the de minimis rate from 10% to 15% in the 2024 update of the Federal Financial Assistance Guide.

If a nonprofit has negotiated an indirect cost rate with the federal government, then departments must use this negotiated rate on federally-funded contracts with that nonprofit. If a nonprofit does not have a negotiated indirect cost rate with the federal government, then departments must use the de minimis rate of 15% on federally-funded contracts with that nonprofit. Departments should verify that the federal grant allows indirect costs to be charged prior to providing funding for the indirect rate within the contract.

When using federal funding, departments must abide by federal standards when setting indirect rates. General Fund contracts do not need to adhere to the de minimis rate established by the federal government. If there is no federal funding in a contract, departments have discretion to match a nonprofit's negotiated indirect rate with the federal government (if relevant) or may apply a different rate according to department policies.

The City has not established a uniform indirect rate for General Fund contracts. Departments have discretion to establish a single indirect rate used for all contracts and/or to negotiate with individual contractors to establish an indirect rate.

Reference: OMB Uniform Guidance Part 200 Subpart F Section 200.14 Indirect Costs – De Minimis Rate.

Capital Expenditures

Allowable Direct Cost.

Capital expenses, including capital improvements, are allowable unless prohibited by City Charter or a federal awarding agency.

OMB states that certain capital expenditures for general purpose land, buildings or equipment are unallowable except when approved in advance by the awarding agency. In such cases where federal funds are awarded to nonprofit service providers and the awarding agency has not explicitly allowed the use of these funds for general purpose capital expenditures, these costs are unallowable.

City Charter prohibits the use of Children's Fund for capital expenditures. The Department of Children, Youth and Their Families includes all associated costs, including mortgage interest costs and depreciation, in this prohibition.

For General Fund contracts and grants, and federally-funded contracts and grants where such costs have been explicitly allowed by the awarding agency, the costs are only allowable with pre-approval by the department. Departments may set funding caps and may require justification and other documentation prior to confirming costs in the grant or contract budget. Allowability does not guarantee funding for capital expenditures. Departments may make choices about the budget items they prioritize for funding.

Capital expenditures must always be considered direct costs. If the building is used by multiple programs, the costs should be allocated using a reasonable methodology.

Reference: OMB Uniform Guidance Part 200 Subpart E Section 200.439 Equipment and Other Capital Expenditures.

Mortgage Principal

Not Allowable.

Principal mortgage costs are not allowable in City contracts or grants. Instead, the cost of the principal can be recovered through depreciation (see below).

Reference: OMB Uniform Guidance Part 200 Subpart E Section 200.436 Depreciation.

Mortgage Interest Fees

Allowable Direct Cost.

With certain restrictions, mortgage interest fees are allowable in City contracts and grants with nonprofits. To be considered allowable, the contract and/or grant must explicitly state this type of expense will be included in the budget and is allowable.

The cost of mortgage interest fees must also be reasonable, meaning they are ordinary, necessary, and in line with fair market value for comparable space. To be considered reasonable, grantees and contractors must demonstrate that the expense being charged to the City aligns with fair market value by providing quotes or similar cost-per-square-foot estimates for three comparable spaces. Departments should verify fair market value prior to budget approval, and may re-verify annually. If the mortgage interest expense exceeds fair

market value, departments must cap allowable payments at fair market value to conform to the reasonable standard.

Mortgage interest fees are always direct program costs. If the building is used by multiple programs, the costs should be proportionally allocated to programs, administrative and fundraising cost centers according to actual usage by each cost center. Departments may request additional documentation necessary to verify the proportional share of space used for funded programs, or to verify fair market value of space.

For facilities acquisitions (excluding renovations and alterations) costing over \$10 million where the Federal government's reimbursement is expected to equal or exceed 40% of an asset's cost, the nonprofit organization must prepare, prior to the acquisition or replacement of the capital asset(s), a justification that demonstrates the need for the facility in the conduct of federally-sponsored activities. Upon request, the needs justification must be provided to the Federal agency with cost cognizance authority as a prerequisite to the continued allowability of interest on debt and depreciation related to the facility.

Mortgage interest fees are unallowable in the following circumstances:

- Interest associated with subsequent loans against property for uses other than occupancy (i.e., a second mortgage) is unallowable.
- Interest attributable to a fully depreciated asset is unallowable.
- Interest in connection with acquisitions of capital assets that occurred prior to September 29, 1995 is unallowable.

Reference: OMB Uniform Guidance Part 200 Subpart E Section 200.449 Interest.

Depreciation

Allowable Indirect Cost.

Depreciation, both for real property and for equipment of over \$5,000 per unit, is an allowable cost. Depreciation is an indirect expense, which may be allocated to programs using a consistent and reasonable methodology.

To approve inclusion of depreciation in a nonprofit contract or grant budget, City departments should review a depreciation schedule provided by the nonprofit. Charges for depreciation must be supported by adequate property records, and physical inventories must be taken at least once every two years to ensure that the assets exist and are usable, used, and needed. In addition, adequate depreciation records showing the amount of depreciation taken each period must also be maintained.

Any portion of the property purchased using either federal or City General Fund dollars must be excluded from depreciation schedule. For example, if the City provides \$500,000 in capital investment for a \$1,000,000 building, the depreciation schedule should exclude the \$500,000 in City-funded capital. Nonprofits must note when City or federal sources funded any portion of capital costs for property.

Per Federal guidelines, a cost may not be treated as a direct cost if any other cost incurred for the same purpose, in like circumstance, has been allocated as an indirect cost. However, there may be circumstances where indirect costs like depreciation may be allowable as direct costs. Such special circumstances must be evaluated on a case-by-case basis. Items generally designated as indirect costs may be treated as direct costs if incurred for different purpose or in unlike circumstances. These costs may be charged directly when:

- The cost can be accurately identified with the specific cost objective;
- The cost is required by the scope of the project;
- The specific type and nature of the cost is significantly greater than ordinarily required by a sponsored project; and
- The cost is clearly disclosed and fully justified in the proposal budget and approved by the City in the grant or contract.

Reference: OMB Uniform Guidance Part 200 Subpart E Section 200.436 Depreciation.