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## Horizon 2020 internal cost allocation

### Executive Summary

In companies that maintain their own research departments and infrastructure, the services provided by these departments are often jointly utilized by different organizational units, whereby the expenses incurred are allocated internally according to use in an established, experience-based, and plausible/demonstrable cost allocation. The rules currently applying to this internal cost allocation in Horizon 2020 are considerably stricter than they were in FP7.

The common practice of using average costs and unit costs, which often include parts of personnel costs, is not possible any longer in H2020. Internally invoiced services can only be billed as direct costs within H2020 if they are directly measureable and verifiable. Personnel costs have to be identified according to H2020 eligibility rules, invoiced as “personnel costs” and reported using time sheets - even if they only account for a very small fraction of the internally invoiced services overall.

For project participants, these new rules represent major challenges when it comes to evaluating and invoicing incurred expenses and thus lead to a loss of reimbursable costs. As a consequence, this may lead to increased research costs if services that have so far been provided internally have to be purchased from external providers in order to be able to have the respective costs reimbursed within the project.

## Internal cost allocation at a glance

**Research infrastructure** like large devices, high-performance computers and animal housing facilities are often **jointly used** by several (research-) departments of one organization or company and are thus **mostly organised as so-called “Core Facilities” - a form of centralised infrastructure**. These Core Facilities provide other organizational units (e.g. different divisions or institutes) with infrastructures and services. By doing so, they regularly invoice **“package prices”** like fixed hourly rates for the usage of devices, which are made up of different elements of costs (amortization charges, maintenance costs, expendables, personnel costs, etc.).

*Examples:*

- *hourly rate for the usage of a large device or laboratory*
- *fixed price per laboratory test carried out*
- *fixed price per animal species (costs relating to animal care/week)*

In case internally invoiced services are utilized in the course of a **research project**, the question arises, whether the established practice within organisations for calculating costs complies with the **criteria of the funding body** as regards the **eligibility of costs**.

## Internal cost allocation in FP7

According to the rules of FP7, internally invoiced costs can be calculated in the form of **average costs** if it is difficult to measure the actual costs or the actual time exposure. The calculation of average costs has to be based on the actual costs as well as on **objective, measurable and verifiable criteria** and the use of the payments for the project needs to be documented correctly. Non-refundable costs (e.g. VAT), overhead costs and profit margins must not be included in the average costs and unit costs.

Unit costs, which also include a certain part of personnel costs (e.g. for technicians, who conduct tests) are considered eligible under the **cost category “other direct costs”** within FP7. In this case it is not required to demonstrate the actual time exposure through time sheets for the persons involved.

In case employees of other organizational units provide specialised services for the project, the relating costs qualify as “internally invoiced personnel costs”. They have to be calculated according to the FP7 requirements for personnel costs and documented by time sheets over the entire working period (full time documentation).

## Internal cost allocation in Horizon 2020

In Horizon 2020 the eligibility of internally invoiced costs is regulated by much stricter requirements compared to FP7. Internally invoiced costs can only be considered as direct costs if they are directly measurable and verifiable and if their calculation is in line with the funding criteria of the Grant Agreement. The billing of internally invoiced average costs is thus excluded.

Another new feature is that internally invoiced costs need to be broken down in budget categories. As a consequence - unlike in FP7 - personnel costs are not allowed to be included in the category "other direct costs" any longer. Within Horizon 2020, internally invoiced personnel costs always need to be calculated according to H2020 rules, reported by time sheets (demonstrating the working time spent on the project) and declared in the category "personnel costs" within the cost sheet.

In order for the costs to qualify as measurable and verifiable, it is necessary to record and expressly indicate the project-relatedness and the utilization period on the invoice.

*Example (see Annotated Model Grant Agreement, p. 84):*

- *Internal invoice for 16 hours of a technician for conducting an analysis and 10 hours of proportional depreciation charges of the testing facilities.*

## Consequences and Concerns than need to be addressed

The Horizon 2020 rules on internal cost allocation were criticized by several organizations for lacking in practical relevance and being hard to administrate.

In January 2016, a group of 620 universities and research organisations under the leadership of the Helmholtz-Association published a declaration entitled "**Joint Statement on the current problem of internal cost allocation (ICA) in Horizon 2020**". A similar declaration had already been published by the Helmholtz-Association in October 2015.

### Major points of concern:

- The new provisions (inadmissibility of unit costs, reporting obligations concerning working time) represent a **setback compared to FP7** and **run contrary to simplification efforts**.
- There is a risk that excellent "**Core Facilities**" of research organisations will **not take part** in H2020-projects any longer, as an adaption of the prevailing cost allocation scheme is too complex and laborious for many organisations.
- If services that have previously been provided internally were to be outsourced to external providers, not only would the **costs** increase in many cases (as external providers often charge higher costs than departments from within the organization), but there would also be a risk of **losing quality**.

### Possible solutions:

In order to remedy this problem, Chambers recommend the establishment of an accountancy and eligibility of total actual internal cost invoicing and the acceptance of internally invoiced costs as packages under the category "other costs".

For the purpose of simplification, Horizon 2020 rules should accept the charging of documentable and plausible average costs, as they are accepted in many national funding programmes as a practical approach applied in consultation with the respective funding body. This approach benefits both the funding body and the project partners as a means of balancing accountability, adherence to rules, transparency, and simplicity of documentation and reporting. In the context of European steel research, this approach using average costs has been acknowledged as eligible and accepted by European Commission auditors. In this sector, as in the life sciences, many different material samples are treated individually in slightly altered processes in a lab to establish the desired material properties or characteristics.

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