

CAS Best Practices Manual
For Reviewing Institutions of Higher Education
Long-Form Facilities & Administrative
Cost Rate Proposals

***U.S. DEPARTMENT OF HEALTH AND HUMAN SERVICES
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**CAS BEST PRACTICES MANUAL FOR REVIEWING
INSTITUTIONS OF HIGHER EDUCATION LONG-FORM FACILITIES AND ADMINISTRATIVE
COST RATE PROPOSALS**

I. INTRODUCTION

This best practice manual (the manual) was developed to assist Cost Allocation Services (CAS) staff in reviewing and analyzing Institutions of Higher Education Facilities and Administrative (F&A) cost rate proposals prepared using the long-form format. The manual addresses a number of important issues and subject matters and presents CAS best practices that should be followed during a review. Alternative approaches and allocation methods are presented and discussed as appropriate. While this manual is reasonably detailed and comprehensive, it is not intended to be a substitute for professional experience and judgment, nor does this manual set policy.

The Office of Management and Budget (OMB) issues cost principles for all Federal agencies that sponsor research, training and other work at institutions of higher education. Title 2 in the Code of Federal Regulations (2 CFR), Part 200, Subparts A to F and Appendix III (hereinafter referred to as “the Cost Principles”) establishes principles for determining costs applicable to grants and contracts with educational institutions. In general, the Cost Principles, among other things, identify, define and discuss the major functions of an institution of higher education, F&A cost pools, the allocation distribution bases, and the allowability of 55 selected items of cost. HHS adopted the Cost Principles at Title 45 of the Code of Federal Regulations, Part 75 (45 CFR 75). There have been numerous revisions to the Cost Principles since the inception of OMB Circular A-21 (the Circular) in 1958. Prior to 1979, the Circular permitted considerable flexibility in the allocation of costs. That flexibility encouraged numerous interpretations of the cost principles which were not originally intended. On March 6, 1979, OMB revised the Circular with many significant and broad changes. On December 11, 1979, the Department's Office of Grant and Contract Financial Management (OGCFM) issued interpretations (Questions and Answers) of the revised Circular. Those interpretations were widely disseminated to the university community and are considered Department policy, to the extent that they have not been superseded. CAS staff should therefore be familiar with the interpretations.

Subsequent revisions to the Circular are highlighted below:

August 3, 1982:

- Modified the procedures for allocating salary costs.
- Allowed interest costs on buildings and equipment acquired or completed on or after July 1, 1982.

December 2, 1986:

- Established a fixed allowance on the reimbursement of costs associated with the administrative activities of academic department heads, faculty and other professional research and instructional staff. This fixed allowance was a departure from the Circular's normal cost reimbursement concepts.

October 1991:

- New unallowable costs were added to the selected items of costs. In addition, provision was made for refunds to the Federal Government for unallowable costs which were included in prior F&A cost rates.
- A cap on administrative costs (General Administration, Departmental Administration and Sponsored Projects Administration) was imposed. These costs were limited to 26 percent of modified total direct costs (MTDC) for all grantee fiscal years beginning after October 1, 1991. Further, grantees could not change their method of accounting or cost allocation methods, which were in use at May 1, 1991, if such a change would shift costs from capped pools to uncapped pools or from F&A to direct costs. Provisions were made for grantees to petition their cognizant agencies for exceptions to this requirement.
- One of the revisions specified that costs assignable to activities sponsored by industry, foreign governments or other sponsors shall not be shifted to Federally sponsored agreements.
- A requirement was imposed on the 99 largest federally funded colleges and universities that required them to "expend currently, or reserve for expenditure within five years, the portion of F&A cost payments made for depreciation or use allowances under sponsored research agreements...to acquire or improve research facilities".

- Finally, grantees would be required to submit a certification with each proposal that certifies under penalty of perjury that the proposal has been reviewed, contains no unallowable costs, that the costs are allocable to Federal agreements and the proposal is prepared using the same accounting practices disclosed in the DS-2 (if applicable)

July 1993:

- Two F&A cost categories were defined; 1) Administrative which includes General Administration, Departmental Administration, Sponsored Projects Administration, Student Administration Services, and any other categories not defined as Facilities costs and 2) Facilities which includes Depreciation and Use Allowances, Operations and Maintenance, Interest and Libraries.
- The administrative cap of 26 percent includes Student administration Services costs.
- The definition of University Research was modified so that University Research is combined with Sponsored Research under Organized Research, eliminating potential mismatching of pool and base costs.
- The predominant use methodology for allocating space related costs was eliminated and a new method for allocating joint use space was implemented.
- An alternative method for administrative costs was provided. Under this method, a grantee could elect to take a rate which is the lesser of 24 percent or 95 percent of the total rate for their Administrative components, with only minimal documentation in support of the Administrative components.
- The threshold for use of the simplified "short-form" methodology was raised from \$3 million to \$10 million.
- The MTDC distribution base was defined.
- The use of multiple year predetermined rates was stated as the preferred methodology.
- Additional language was incorporated to better define General Administration, Departmental Administration and Operations and Maintenance.
- Finally, there was new language with regard to allocation and documentation standards, consistency, medical liability insurance and tuition remission.

January 1995:

- Educational institutions were made subject to four Cost Accounting Standards (CAS), effective January 1995, per a Final Rule published in the Federal Register in November 1994. The four Cost Accounting Standards are CAS 9905.501 - consistency in estimating, accumulating and reporting costs; CAS 9905.502 - consistency in allocating costs incurred for the same purposes; CAS 9905.505 - accounting for unallowable costs; and CAS 9905.506 - consistency in the selection and use of a cost accounting period.

May 1996:

- The four Cost Accounting Standards were incorporated in the Circular along with the associated administrative requirements promulgated by the Cost Accounting Standards Board (CASB).
- Major institutions (those that receive aggregate sponsored agreements totaling \$25 million or more subject to the Circular during the most recently completed fiscal year) were required to file a Disclosure Statement (DS-2) explaining their cost accounting practices.
- The term “indirect costs” was replaced by the term “Facilities and Administrative (F&A) costs”.
- Special cost analysis studies for libraries, student services and utility costs were eliminated effective July 1, 1998, although special cost analysis studies for libraries were subsequently reinstated.
- A new requirement was made for funding agencies to use F&A rates in effect at the time of an initial award throughout the life (competitive segment) of the sponsored agreement.
- OMB Circular A-88 was rescinded and cognizance for negotiations / audits was established through the Circular.
- Dependent tuition benefits were eliminated as allowable expenses.
- The HHS interpretation for conversion from use allowance to depreciation was incorporated in the Circular.
- The definition of capital equipment was amended by increasing the capitalization threshold to the lesser of the amount used for financial statement purposes or \$5,000. Also, useful life for capital equipment was defined as one year or more.
- Finally, new provisions were incorporated related to interest expenses. A lease / purchase analysis was required for facilities costing over \$500,000 and a cash flow analysis was required for debt arrangements over \$1 million, unless the institution used at least 25 percent equity financing.

June 1998:

- A provision for reviewing the reasonableness of costs associated with large research facilities was incorporated.
- A Utility Cost Adjustment (UCA) of 1.3 percent was provided in lieu of the special utility cost studies for institutions that had used such studies in negotiating their most recent F&A rates.
- Criteria were specified to provide guidelines under which the salaries of administrative and clerical staff may be treated as direct costs.
- A new option was provided for the computation of F&A rates under the simplified (“short-form”) method using a modified total direct cost base.
- The language on depreciation was modified to require that the depreciation methods used to calculate the depreciation amounts for F&A rate purposes shall be the same methods used by the institution for its financial statements.
- Additional requirements were made for institutions choosing to use the building componentization methodology for depreciating buildings.
- The language on use allowance was changed to limit the recovery of costs to the acquisition costs of the assets.
- A provision was added to recognize the gains / losses on the final disposition of depreciable property.
- Finally, travel and subsistence costs of trustees were made allowable.

August 2000:

- OMB approved a standard format for submission of long-form F&A proposals. This is incorporated in the Circular as Appendix C.

May 2004:

- Allows homeland security costs, costs of A-133 audits, required and reasonable bonding costs, advisory council costs and training costs that are provided for employee development.
- Divides donations between donated services and donated property.
- Disallows interest on fully depreciated assets and on debt incurred to finance or refinance assets re-acquired.
- Prohibits interest on re-acquired assets after applicable dates.
- Disallows settlement expenses related to terminations of sponsored agreements when the termination is for default.
- Adds more clarity to allowable and unallowable patent costs and to professional service costs.
- Defines and sets parameters on the allowability of publication and printing costs.
- Adds more clarity to rental costs of buildings and equipment and adding more clarity to royalties and other costs for use of patents.
- Defines Idle facilities and idle capacity and establishes parameters on allowability.
- Requires specialized service facilities to adjust rates charged at least biennially taking into consideration over/under applied costs of the previous period(s).
- Defines allowable tuition remission and other support by emphasizing the relationship to Federally-sponsored research projects.
- Grants conditional exemptions from certain OMB circulars for certain Federal programs with statutorily authorized consolidated planning and consolidated administrative funding that are identified by a Federal agency and approved by the head of the Executive department or establishment as authorized by OMB.

In December 2013, OMB issued final guidance to supersede and streamline OMB Circulars A-21, A-87, A-110, and A-122 (which have been placed in OMB guidance); Circulars A-89, A-102, and A-133; and the guidance in Circular A-50 on Single Audit Act follow-up; into one consolidated format. This final guidance was located in 2 CFR, Part 200. Future reform efforts may eventually seek to incorporate the Cost Principles for Hospitals into the guidance. The purpose was to:

1. Eliminate duplicative and conflicting guidance;
2. Focus on performance over compliance for accountability;
3. Encourage efficient use of information technology and shared services;
4. Provide for consistent and transparent treatment of costs;

5. Limit allowable costs to make best use of Federal resources;
6. Set standard business processes using data definitions;
7. Encourage non-Federal entities to have family-friendly policies;
8. Strengthen oversight; and
9. Target audit requirements on risk of waste, fraud, and abuse.

OMB instructed Federal agencies to implement the guidance by promulgating regulations to be effective by December 26, 2014.

In December 2014, OMB and Federal agencies issued an interim final rule implementing 2 CFR 200 as of December 26, 2014. HHS implemented the new regulations at 45 CFR 75. 2 CFR 200/45 CFR 75 established uniform administrative requirements, cost principles, and audit requirements for Federal awards to non-Federal entities. The entire document is hereinafter referred to as “the Cost Principles”.

The objective of the Cost Principles is to establish principles for determining the allowable costs incurred by non-Federal entities under Federal awards. The Cost Principles are designed to provide that Federal awards bear their fair share of costs recognized under these principles except where prohibited or restricted by statute. These principles are for the purpose of cost determination and are not intended to identify the circumstances or dictate the extent of Federal Government participation in the financing of a particular program or project.

The Cost Principles contains six subparts:

- Subpart A – Acronyms and Definitions (the definitions are a key component of the Cost Principles)
- Subpart B – General Provisions
- Subpart C – Pre-Federal Award Requirements and Contents of Federal Awards
- Subpart D – Post-Federal Award Requirements
- Subpart E – Cost Principles
- Subpart F – Audit Requirements

The negotiator should particularly familiarize themselves with Subparts A, B, and E.

Significant changes to Institutions of Higher Education contained in these Cost Principles include the following:

- Appendix III to Part 200—Indirect (F&A) Costs Identification and Assignment, and Rate Determination for Institutions of Higher Education (IHEs) was added to provide criteria for identifying and computing indirect (F&A) rates at IHEs as previously contained in OMB Circular A-21.
- A new provision was added that allows any non-Federal entity that has a federally negotiated indirect cost rate to apply for a one-time extension of their current negotiated indirect cost rates for a period of up to four years. The extension is subject to the review and approval of the cognizant agency for indirect costs. If an extension is granted the non-Federal entity may not request a rate review until the extension period ends. At the end of the 4-year extension, the non-Federal entity must re-apply to negotiate a rate.
- Provisions were added to extend to all IHEs the provisions previously extended only to the 66 IHEs listed in Exhibit B of the Circular that allow for recovery of increased utility costs associated with research. A utility cost adjustment may be included in the negotiated indirect cost rate of the IHE for organized research, per the computation alternatives contained in the Cost Principles which includes a relative energy utilization index (REUI).
- The amount recoverable for the utility cost adjustment was limited to an amount equal to 1.3 percentage points of the IHE's indirect cost rate until such time as OMB and Federal agencies can better understand the cost implications of full reimbursement of actual costs and the potential implication for Federal programs.
- Information technology systems have been included in the definition of equipment. Software is included in the definition of information technology systems. The maximum capitalization level of \$5,000 now applies to software. This definition encompasses both purchased software with a unit cost greater than \$5,000 and internally developed software projects with a cost greater than \$5,000 (or a lesser level established for financial statement purposes).
- The threshold for IHE required to file a Disclosure Statement (DS-2) explaining their cost accounting practices was raised to an aggregate amount of Federal awards totaling \$50 million or more during the most recently completed fiscal year that are subject to the Cost Principles in Part 200 of 2 CFR.

F&A costs are those expenses that benefit common activities and therefore cannot be readily assigned to a specific cost objective or project. At educational institutions such costs are classified into the following categories: (1) building and equipment depreciation; (2) operation and maintenance (O&M) (including utility expenses); (3) interest associated with the acquisition of certain capital construction and equipment; (4) general administration and general expenses (GA); (5) departmental administration (DA); (6) sponsored projects administration (SPA); (7) library, and; (8) student administration and services (SAS). F&A costs are apportioned between organized research and the other major functions of a university, such as instruction, other sponsored activities and other institutional activities, based on various allocation procedures prescribed in the Cost Principles. The portion of F&A costs identified with organized research is further distributed to individual research projects through the application of an F&A cost rate(s). Where necessary, an F&A cost

rate is also established for the instruction function and for "other sponsored programs (or activities)". The preparation of an F&A cost proposal and the maintenance of its subsystems is a significant undertaking, and at many large institutions requires the efforts of a full-time staff and in some instances involves the assistance of outside consultants. The importance placed upon the development of a comprehensive F&A cost proposal, including the development of special costing studies and the use of outside consultants, affects the time and degree of sophistication required by CAS staff to effectively evaluate the cost proposal and related documentation.

The decision to perform an in-depth review and analysis by the CAS (including the need for team reviews) will be influenced by (a) deviation from the standard allocation methods prescribed in the Cost Principles, (b) use of specialized costing studies, (c) use of outside consultants, (d) excessive costs assigned to research compared to the regional or national norm, (e) inadequate documentation, (f) overall level of the proposed rate, (g) total dollars at risk, (h) rate trends, (i) Disclosure Statement (DS-2) inadequacies or noncompliance and (j) Subpart F of the Cost Principles or other Federal audit findings.

Questions or clarifications regarding the information presented in this best practices manual should be directed to Michael Leonard, College and University National Specialist, by e-mail michael.leonard@psc.hhs.gov. Questions specific to an institution should be directed to the cognizant CAS Regional Office.

II. PRELIMINARY REVIEW

A. GENERAL REVIEW

STEPS

1. Determine whether the proposal package is complete, in sufficient detail to permit an adequate review, and is in a format that can be readily followed by the CAS.

COMMENTS

The proposal package should include:

The proposal itself, submitted in the Standard Format prescribed in the Cost Principles as per Section E of Appendix III, found on OMB's website:

https://www.whitehouse.gov/omb/grants_forms which includes detailed schedules on the composition and allocation of each F&A cost pool, and subpools as applicable.

Audited financial statements.

A detailed and understandable reconciliation between the proposal and financial statements, showing and explaining each reclassification and adjustment to the financial statement accounts.

An explanation should be provided for any significant increases in individual rate components. A significant increase occurs when the proposed rate component increases

STEPS

COMMENTS

more than 10 percent from the negotiated rate component published in the negotiation component agreement and the rate component is at least 10 points on the rate.

Any information specifically requested by the CAS in prior agreements.

A certificate of F&A costs, in accordance with the Cost Principles Section F of Appendix III, certifying that the proposal has been reviewed and that the costs are allowable and allocable.

Single audit report (Subpart F of the Cost Principles) for the base year of the proposal. If not available, the most recent single audit report should be requested. The single audit report may have findings with regard to internal controls, systems deficiencies, etc.

Methodologies and results for deviations from standard methods prescribed in the Cost Principles.

The methodology and results of any review for unallowable/unallocable costs.

STEPS

COMMENTS

2. Review the prior negotiation workpapers and determine the following:
 - a. When was the last on-site review conducted?
 - b. Determine when was the last single audit submitted and what were the results of the audit?
 - c. What problems were found and adjustments made in prior negotiations? Were corrections made in the current proposal?
 - d. Were fringe benefits, off-campus or other special rates negotiated?
 - e. Is a Disclosure Statement (DS-2) required?
 - f. Has the University complied with all conditions of any advance agreements?
 - g. If an F&A or a fringe benefit fixed rate was negotiated, does the carry-forward amount in the current proposal agree with the prior written carry-forward agreement?
3. Are there any areas of the proposal that appear out of the norm and that are not fully explained or discussed in the proposal package or the

Were there any findings affecting the F&A cost rate proposal? If so, obtain the details and determine if the issues impact the F&A rate.

If the corrections were not made, appropriate adjustments should be made to the current proposal.

The Cost Principles 2 CFR part 200.419 provides the guidelines for determining if an institution must submit a DS-2.

STEPS

COMMENTS

prior years' workpaper files?

4. Determine the areas of the proposal that appear to require an in-depth review and/or an on-site review.
5. Determine whether an audit of the proposal is needed.
6. Determine whether the institution is proposing any rate increases beyond the rate based on historical costs of the base year.
7. Determine whether off-campus or other special indirect cost rates are needed.
8. Determine the treatment of fringe benefits.
9. In accordance with the Cost Principles, Appendix III, Section C.8., the administrative

On-site reviews are usually needed to evaluate F&A cost proposals from major institutions.

As a general rule, an audit of an F&A cost proposal should be requested only where there are very large amounts involved and there appear to be serious problems with the proposal. If an audit is requested, the request should indicate the specific area(s) of the proposal the audit should cover. Also, to the extent possible, the negotiator should work closely with the auditors in planning and conducting the audit.

See Section XII.J. for guidelines on evaluating rate projections and for the required documentation.

If these rates were established in the past, they will likely also be needed in the future. Also, information provided by Federal agency grant or contract offices may indicate the need for a special rate. In planning the extent of analysis necessary for these rates, consider the amount of Federal dollars to which the rates apply. These rates may require in-depth reviews.

See Section XII.A.

STEPS

costs charged to sponsored agreements shall be limited to 26% of MTDC for the total of GA, DA, SPA, and SSA. Determine whether the institution has properly implemented the administrative cap.

10. Section C.9. of Appendix III of the Cost Principles provides an alternative method for administrative costs whereby the institution may claim a fixed allowance for the "Administration" portion of F&A costs provided there have not been certain accounting or cost allocation changes. The allowance claimed could be either 24% of MTDC, or a percentage equal to 95% of the most recently negotiated fixed or predetermined rate for the administrative cost pools, whichever is less.

COMMENTS

B. RECONCILIATION OF COST PROPOSAL TO FINANCIAL STATEMENTS

It is very important for the negotiator to review the university's reconciliation of the F&A cost proposal to the audited financial statements. This process is essential to the negotiation and must be completed on each proposal. The reconciliation process will provide insight into the university's organizational structure, accounting system and costing methodologies that are critical to the proposal review process. The reconciliation must be completed by the university and submitted with its proposal as required by the Cost Principles' Standard Format. If the university has not completed the reconciliation, it must be notified immediately to do so. The proposal is considered delinquent until the reconciliation has been received by the CAS.

STEPS

1. Evaluate the adequacy of the institution's reconciliation of the proposal to the audited financial statements.

COMMENTS

The first step is to reconcile total costs, both allowable and unallowable, to the total costs shown on the audited financial statement. This includes both restricted and unrestricted accounts and should provide a reconciliation of individual cost pools and direct cost bases, such as general administration and general expenses, operations and maintenance, instruction, organized research, etc., to the financial statements. In some cases, costs shown on the audited financial statement may include organizations that are not subject to the F&A cost rate computation. For example, many universities have affiliated hospitals. In these cases it may be necessary to exclude all costs not pertaining to the institution under review. However, if the affiliated organization is receiving a service or benefit from the institution, the associated costs must be assigned to that organization.

STEPS

2. Analyze all supporting schedules used in the reconciliation process.
3. Once the negotiator is assured that the total costs, direct and F&A, included in the F&A cost proposal reconcile to the audited financial statements, he or she should analyze the adjustments for unallowable and extraneous costs that should either be excluded from the proposal or allocated their share of F&A costs.
4. Analyze and verify the accuracy and necessity for adjustments and reclassifications.

COMMENTS

There may be subsidiary schedules included as part of the reconciliation process. Frequently, a State university is part of a larger State system. In these cases the negotiator must review the applicable central administration cost distribution schedules for reconciliation purposes.

The negotiator must evaluate all excludable costs to assure that they are not to be burdened F&A costs. The university must not eliminate functions that should receive an allocation of G&A, O&M or other F&A costs (e.g., fund raising, services to outside organizations, etc.). Evaluations must also be made for exclusions and for tuition remission, stipends and fellowships. A frequent error found in reconciliations is the deletion of all subcontract costs, rather than only the amounts over the first \$25,000 or the deletion of costs associated with a medical practice plan (see Section XII.C. for further discussion of medical practice plans). In any case, the negotiator must be careful to assure that all material eliminations are appropriate.

The negotiator must understand every material reclassification and why it is taking place. Understanding the reclassification process is an important part of the review. Extra attention and analysis should apply to any reclassifications or adjustments resulting in reductions to the Organized Research direct cost category. A reclassification for cost sharing should be revealed in the reconciliation and be further analyzed as considered appropriate. Unallowable and unallocable costs (e.g., bad debts,

STEPS

COMMENTS

scholarships, etc.) should always be eliminated from the F&A cost pools before the pools are allocated. However, unallowable activities that require an allocation of F&A costs (e.g., fund raising, public relations, alumni activities, etc.) should be reclassified to "other institutional activities" and receive their proper allocation of F&A costs based on benefits received. Unallowable activities usually include salaries and wages, occupy space and generate administration.

C. REVIEW OF DIRECT COST BASE

The direct cost base should be a major area for review because of its impact on the F&A cost rate calculation. A base that is understated will result in an inflated F&A rate. All modified total direct costs of functions benefiting from the F&A cost pools must be included in the applicable base in the rate computations regardless of the actual recovery of F&A costs. As described in Section II.B. above, all costs reclassified from one function to another must be analyzed. A thorough analysis should be made to insure that the salaries and wages for all occupants of organized research space have been included in the organized research direct cost base. Imputing salary for those room occupants who are not paid by the institution may be appropriate.

STEPS

COMMENTS

1. Analyze and verify the accuracy of the costs assigned to each functional direct cost base.

The primary schedule used in the review of the university's base is the summary of reclassifications and adjustments. Once the costs in the financial statements have been reconciled to the cost categories in the proposal the base analysis can begin.

STEPS

2. Verify that all costs for each function have been included in the rate computation.

COMMENTS

The following is a list of activities which normally benefit from F&A costs:

Unrestricted funds, such as Instruction and University-funded research (commonly called Departmental Research). See DA Section.

Restricted funds, such as Sponsored Research, and other sponsored activities supported by private grants, gifts, endowments, etc.

Students working on sponsored projects, their thesis or receiving training. (Also see Tuition Remission Section XII.E)

Voluntary services (e.g., voluntary faculty at medical schools).

Cost sharing and matching.

Unallowable activities, such as fund raising, public relations, alumni activities, etc.

Projects funded and performed by other organizations on university's premises utilizing university services.

STEPS

COMMENTS

3. Analyze all functional base adjustments and determine the appropriateness of each adjustment. Does the final distribution base conform to the MTDC base in the Cost Principles? Does the proposal clearly state and define the exclusions from the base?

Other Institutional Activities (Auxiliary Operations) such as dormitories, athletic stadiums, bookstores, dairy farms, food services, etc. unless they incur their own facilities or administrative costs.

Visiting scientists from other institutions or foreign countries with or without their own funding.

Other outside users of the institution's services.

The Cost Principles 2 CFR part 200.68 states that modified total direct costs consist of all direct salaries and wages, applicable fringe benefits, materials and supplies, services, travel, and subawards up to the first \$25,000 of each subaward (regardless of the period of performance of the subawards under the award). MTDC excludes equipment, capital expenditures, charges for patient care, rental costs, tuition remission, scholarships and fellowships, participant support costs and the portion of each subaward in excess of \$25,000. Other items may only be excluded when necessary to avoid a serious inequity in the distribution of indirect costs, and with the approval of the cognizant agency for indirect costs. (The exclusion for rental costs relates to building rental costs, not equipment rental costs.)

STEPS

4. Determine that the university has accurately identified and included all cost sharing in the organized research direct cost base. (See XII.F)

COMMENTS

Although most mandatory cost sharing requirements have been eliminated, there is still a widespread belief among faculty members that a high degree of committed cost sharing insures favorable review of research project proposals by awarding agencies. The negotiator must examine and ensure that all cost sharing, both mandatory and voluntary committed, has been included in the direct cost base. The negotiator should obtain copies of institution's cost sharing policies. The negotiator may need to review a number of grant files in departments performing a significant amount of Federally sponsored organized research to determine if there is voluntary committed cost sharing in either the proposed budget or narrative description. Based on this analysis the negotiator should determine if the committed cost sharing in the F&A cost rate proposal is reasonable.

If mandatory or voluntary committed cost shared effort is not included in the Organized Research base, then the organized research space associated with this cost shared effort should be adjusted accordingly. It is essential that there is consistency between the classification of space for the allocation of the cost pools and the classification of the users of the space in the direct cost base.

The salary in excess of the NIH salary limitation must be included in the appropriate base for the F&A rate calculation according to where the individual effort was performed. It should **not** be considered voluntary

STEPS

COMMENTS

uncommitted cost sharing and eliminated from the base. For instance, if an individual worked on an Organized Research project(s), the salary in excess of the NIH limitation related to effort on that project(s) must be included in the Organized Research base. The effort reporting percentages must be applied to total salary including the NIH salary limitation excess. For example if:

Salary in 2016: \$240,000
NIH Salary Cap: \$185,100
Percent of time to award: 25%
Amount of salary paid from award: \$46,275

Then:

Amount that should be in the research base for this effort: \$60,000

This treatment is further supported in the Frequently Asked Questions (FAQ) presented by the COFAR on OMB's Uniform Guidance at 2 CFR 200 published in September 2015 according to the FAQ content found in Appendix III – 3 of that document.

The individuals being paid over the salary limitations are most commonly found at medical schools. Therefore greater attention on this issue should be performed at the medical schools.

5. Verify that research training is consistently treated.

Research training awards may be classified as either organized research or instruction. The important point

STEPS

COMMENTS

6. Identify other areas of inconsistency.

to remember is that the direct cost dollars associated with the research training must be classified consistently to the same function as the space in which the training is conducted. It would not be appropriate, for research training to be classified as instruction, while the space where the research training takes place is classified as organized research.

There are other areas of inconsistency, but the impact on the research F&A cost rate is usually not significant. The primary areas are fringe benefits, subcontract costs and the differences between on-campus and off-campus charges. For example, a university may apply the negotiated rate to subcontracts when subcontract costs, even the first \$25,000, are not included in the MTDC base. These errors are infrequent but they do occur and should be reviewed.

University research refers to all research and development activities that are separately budgeted and accounted for by the institution under an internal application of institutional funds. University research must be combined with sponsored research under organized research for allocation of F&A costs. This should eliminate a potential inconsistency in matching pool and base costs.

D. TREND ANALYSIS

A trend analysis of the university's F&A cost rates, rate components, cost pools, direct cost bases and other factors should be performed during the preliminary review of each long form university cost proposal. A trend analysis can be completed in a short period of time and frequently provides the negotiator with an insight into the direction the university's F&A cost rates are headed and areas where a detailed review is necessary.

STEPS

COMMENTS

1. Complete a detailed trend analysis of the university's F&A cost rates, rate components, cost pools and direct cost bases.

There are at least two types of trend analyses. The negotiator should use the most recent prior proposal in this analysis and may use up to the last three base years of costs to develop a trend analysis.

The first type of trend analysis is simply plotting the raw rate value of each F&A cost pool along with the applicable base involved. This provides the negotiator not only with an indication of where the rate is changing (increasing or decreasing), but should also indicate where the negotiator should spend time reviewing the cost proposal.

In the second type of trend analysis, the negotiator compares the ratio of research participation of each cost pool with that of previous years, and with the ratios for other cost functions. This analysis is used in conjunction with the rate analysis. A comparison of base changes can now be easily made and the consistency between space and assigned costs can be quickly ascertained.

STEPS

COMMENTS

For example, if the ratio of G&A allocated to research is substantially different than the O&M ratio, then the negotiator should review the rationale. This analysis can also reveal if organized research space is increasing at a ratio greater than the increase in the organized research direct cost base. Although this ratio analysis in itself does not mean there is a problem, it supports further analysis.

Often costs appear to be rising at an excessive rate, however, the change in the base must be similarly analyzed and compared. Secondly, because of changes in accounting classifications in recent years (especially in administrative areas) the negotiator must be assured that the comparison of costs between years is consistent. For example, a contracts office or research accounting office might have been included in G&A in one year and in DA, or more frequently SPA, the next.

2. Evaluate the university's justification for any significant changes.

E. COST ACCOUNTING STANDARDS

The cost accounting standards which apply to educational institutions that receive aggregate Federal awards totaling \$50 million or more in Federal awards are (1) consistency in estimating, accumulating and reporting costs, (2) consistency in allocating costs incurred for the same purposes, (3) accounting for unallowable costs and (4) consistency in the selection and use of a cost accounting period. (See cost accounting standards located at 48 CFR 9905.501, 9905.502, 9905.505, and 9905.506)

Educational institutions that receive aggregate Federal awards totaling \$50 million or more subject to the Cost Principles in 2 CFR part 200 during their most recently completed fiscal year shall disclose their cost accounting practices by filing a Disclosure Statement (DS-2). With the approval of the cognizant agency, an educational institution may meet the DS-2 submission by submitting the DS-2 for each business unit that received \$50 million or more in Federal awards. OMB is expected to release a new DS-2 form in calendar year 2017. When the new DS-2 form is available, all IHE required to have a DS-2 are expected to file a new DS-2 updating to the current Cost Principles. They must have the DS-2 on file within 90 days after the new DS-2 form is available. However they may wait to submit the DS-2 to CAS until their next F&A rate proposal submission is due. All DS-2 that are only updated to the new form in order to comply with the current Cost Principles do not need review or approval from CAS. Educational institutions must file amendments to the DS-2 when disclosed practices are changed that have impacts on Federal awards. Amendments to the DS-2 may be submitted at any time. If the change is expected to have a material impact on the educational institution's negotiated F&A cost rates, the revision shall be approved by the cognizant agency before it is implemented.

The negotiator will need to compare the cost accounting policies delineated in the DS-2 to the F&A cost and fringe benefit proposals in order to ensure that the proposals are consistent with the DS-2. Discrepancies will have to be accounted for by the institutions.

F. FILE DOCUMENTATION

The negotiation workpaper files (electronic files within eFlow) should contain sufficient documentation to support the negotiation of the F&A rate. The electronic workpaper files should include, but not necessarily be limited to: excel worksheets and schedules developed during the review, letters/emails to the grantee requesting additional information and their responses, notes to the file, documentation of phone conversations, etc. The electronic file documents should clearly document:

STEPS

COMMENTS

1) The areas of the proposal that were reviewed.

Each cost pool should have a summary narrative for the review and the scope of work. This section should contain the steps taken during the review and the results of the review.

2) The significant areas of the proposal that were not reviewed and why.

If certain cost pools were not reviewed or the scope of the review was limited, document the reasons.

3) Document the methodology used in choosing your space sample.

Explain how you chose your space sample. The documentation should include departments chosen and the rationale behind the choices. Space interview sheets should be included in the electronic file documentation. A detailed analysis of your space sample results should also be included and should clearly support any recommended adjustments.

STEPS

- 4) Document all adjustments that were made to the proposal and the reasons for the adjustments.

- 5) Component worksheets must be included in the file.

- 6) A cost avoidance worksheet must be included in file.

- 7) Required certifications and disclosure statements.

COMMENTS

Explain the results of the review and the negotiation position. Also explain how you arrived at the negotiated settlement. A summary of the negotiated rates should clearly identify the adjustments taken for each pool and for any base adjustments that were made.

A worksheet showing the negotiated rate percentages by component for each rate negotiated must be prepared.

Cost avoidance must be calculated according to CAS policy.

File must include a copy of the Standard Format and the Certification of F & A Costs.

III. DEPRECIATION

Depreciation is the methodology permitted to be used to compensate institutions for the use of their buildings, capital improvements and equipment. The assets must be used, needed in the institution's activities and properly allocable to sponsored agreements. The computation of depreciation is based on the acquisition cost of the asset exclusive of (1) the cost of land, (2) any portion of the cost of buildings and equipment borne or donated by the Federal Government, irrespective of where title was originally vested or where it is presently located, (3) any portion of the cost of buildings and equipment contributed by or for the institution where law or agreement prohibit recovery. Once title passes, assets donated by a third party may be depreciated at their fair market value at the time of the donation. The expenses for depreciation are allocated based on the method detailed in Appendix III Section B.2. of the Cost Principles.

The Cost Principles require that the same methodology be used for computing depreciation for the financial statements and the facilities and administrative cost rate.

STEPS

COMMENTS

1. Determine if depreciation expense is recognized on the audited financial statements.
2. Reconcile the asset costs from the audited financial statements to the F&A rate proposal.

The Federal negotiator should address any concerns about the reasonableness of the depreciation expense shown in the financial statements to the institution's external auditors who are responsible for certifying the adequacy of the institution's financial statements.

The institution should provide a clear reconciliation.

STEPS

3. For each building with a significant amount of building depreciation allocated to organized research, obtain the following schedules showing (1) total original cost by component, if applicable, and the year occupied, (2) costs associated with remodeling and renovations and the years the costs were capitalized, (3) costs that were excluded from the claimed depreciation (4) a listing of useful lives by asset category and (5) an explanation of how the estimated useful life for each component was determined.

COMMENTS

Verify that there was no depreciation associated with buildings or building components that were beyond their useful lives. Determine if appropriate exclusions for federal participation and other exclusions were made.

Determine if there is depreciation included in the proposal that will affect the negotiation of multi-year predetermined rates. For example, are there assets of significant value that will be fully depreciated prior to the end of the multi year cycle? If so, adjustments to the affected years should be made.

The treatment for writing-off the undepreciated balance associated with assets when institutions switch to building componentization must be analyzed. If no useful life remains for any specific component being written-off then the institution may be including the total write-off in one year (the base year). This is a significant issue on buildings 15 years or older as major components within a building have no remaining useful life. Allowing the total undepreciated balance to be written-off in one year could distort the F&A rate. Care must be taken that if the undepreciated balance is allowed to be taken in one year, future years of a multi-year negotiation should be adjusted.

When an institution switches to or utilizes building componentization, a copy of the study methodology, including the procedures and assumptions used in conducting the study, should be obtained.

STEPS

COMMENTS

4. For equipment depreciation, obtain the inventory listings identifying the following attributes: (1) building location (2) responsible department (3) room number, (4) tag number, (5) asset description, (6) year acquired, (7) acquisition cost, (8) estimated useful life, (9) depreciation amount, (10) manufacturer, and (11) funding source.

Determine that there is no depreciation associated with assets that are beyond their useful lives included in the equipment depreciation cost pool. Determine if appropriate eliminations have been made. Confirm that the acquisition costs associated with equipment included in the pool are in accordance with the capitalization policy dollar threshold identified on the last negotiated rate agreement.

Use these listings to choose a sample of equipment to be verified on a site visit. For equipment allocated on a room-by-room basis, analysis should be made to determine that each item of equipment is found in the room listed for that item of equipment. At a minimum, the item should be found in a room that is in the same building and department with the same allocation of space. If there is a significant discrepancy in verifying the equipment by room, then the equipment depreciation expenses must be allocated on a building-by-building or a department-by-department square footage basis.

5. Determine that the costs of assets were properly established.

For a purchased asset, the depreciable cost is the acquisition cost which is the amount paid and posted in the institution's accounting records. Assets donated by an independent third party, may be depreciated on

STEPS

COMMENTS

- estimated fair market value at the time of donation.
- If cost records do not exist, estimated acquisition cost should be based on an independent and professional appraisal. When appraisals are used, care should be exercised to ensure that this valuation reflects estimated cost at the time of purchase and not replacement cost at the time of the appraisal.
6. Determine that land and Federally funded assets (or portion of assets that were Federally funded) have been eliminated from the computation.
- Federally funded assets should be identified by major funding sources (organized research, instruction, and other sponsored activities) and Federal dollars must be eliminated from each function. The adjustment for Federal funded purchases should not be an elimination from the gross (total) university asset account because doing so may result in an excessive amount of the remaining assets being allocated to the organized research function when the allocation of the remaining assets is on a building, department or campus-wide square footage basis. If the university allocates equipment depreciation room by room, this specific functional adjustment is not necessary.
7. Obtain and adjust depreciation amounts associated with assets or parts of assets acquired to meet Federal grantee matching fund requirements.
- When the institution is required to provide matching funds for the acquisition of equipment on research awards, the costs related to the matching requirement must be excluded from the calculation of depreciation in order to avoid a CAS 502 violation for inconsistent costing. Where cost sharing is associated with buildings or equipment on construction awards, the cost shared amount may be depreciated unless specifically

STEPS

COMMENTS

8. Determine that assets acquired on non-Federally sponsored awards have been excluded from the depreciation/use allowance pools.

9. Determine if building componentization was used.

prohibited in the award. Where cost sharing is associated with equipment on instrumentation awards, allowability will be evaluated on a case-by-case basis.

Non-Federally funded assets should be identified by major funding sources (organized research, instruction, and other sponsored activities) and eliminated from each major function. The adjustment for non-Federal sponsored awards should not be an elimination from the gross (total) university asset account. If the university allocates equipment depreciation room by room, this specific functional adjustment is not necessary.

If an institution elects to establish various useful lives for building components, the Cost Principles provide for three general component groupings:

- Building shell (including construction and design costs).
- Building Services Systems (e.g., elevators, HVAC, plumbing, heating and air-conditioning systems)
- Fixed Equipment (e.g., sterilizers, casework, fume-hoods, cold rooms, glassware/washers)

Institutions may group their equipment into the following

STEPS

COMMENTS

asset classes for purposes of applying the restriction:

- Office equipment (e.g., desks, files, typewriters)
- Scientific equipment (e.g., microscopes, spectrometers, dental chairs/treatment units, laboratory benches, x-ray machines)
- Automatic data processing equipment (e.g., central processing units, tape drives, disc drives)
- Transportation equipment (e.g., automobiles, trucks, trailers, motorcycles, airplanes)
- Educational/other academic support equipment (e.g., classroom furniture, audio visual equipment, shop machinery and tools, musical instruments, athletic equipment)

10. Determine that depreciation charges associated with idle facilities have been properly handled. Also, verify that depreciation charges associated with lost or replaced assets have been eliminated.

Idle facilities are unused facilities that are in excess of the organization's current needs. Costs associated with idle facilities are unallowable with the following exceptions:

The facilities are necessary to meet fluctuations in workload, and the facilities were necessary when

STEPS

COMMENTS

	<p>originally acquired; and are now idle because of programmatic requirements (e.g., efforts to achieve more economical operations, reorganizations, terminations or other causes which could not have been reasonably foreseen).</p> <p>Normally the costs of idle facilities are allowable for a reasonable period of time, ordinarily not to exceed one year, depending upon the initiative taken to use, lease, or dispose of such facilities.</p>
11. Determine that the depreciation method used results in an equitable allocation of costs relative to the time periods in which the assets are used.	<p>With very rare exceptions, the Cost Principles require the use of the straight-line depreciation method.</p>
12. Verify the treatment of gains or losses on disposition of plant equipment and other capital assets.	<p>Gains and losses on the sale, retirement or other disposition of depreciable property shall be recognized in the year in which they occur as credits or charges to the asset cost grouping(s) in which the property was included. A gain or loss is the difference between the amount realized and the undepreciated basis of that asset.</p> <p>The gains or losses will not be recognized if the:</p> <ul style="list-style-type: none">• Gain or loss is processed through a depreciation account and is reflected as a component of allowable depreciation;• Property was part of a trade-in (or exchange) of a

STEPS

COMMENTS

13. Compare the allocation of building depreciation with that for O&M. If there are significant differences, determine the reasons.

similar item and the gain or loss was recognized in determining the cost basis of the new asset;

- Loss results from failure to maintain permissible insurance; or

Building depreciation can be allocated on a campus-wide square footage basis or a building-by-building square footage basis. An advanced level (floor-by-floor, room-by-room, project-by-project, etc.) is **not** an acceptable methodology. The negotiator should question the university to determine if a floor by floor, room by room or project by project allocation was made. If yes, the impact should be determined and an adjustment to the proposed rate should be made.

STEPS

14. Examine the treatment of the cost for information technology systems including Wi-Fi infrastructure costs.

COMMENTS

Section 200.33 of the Cost Principles includes information technology systems in the definition of equipment. Section 200.58 of the Cost Principles includes software in the definition of information technology systems. Therefore, the lesser of the capitalization level established by the non-Federal entity for financial statement purposes, or \$5,000 applies to software. This definition encompasses both purchased software with a unit cost greater than \$5,000 and internally developed software projects with a cost greater than \$5,000 (or a lesser level established for financial statement purposes).

Section 200.58 of the Cost Principles also states that information technology systems include computing devices, ancillary equipment and firmware. The Wi-Fi information technology infrastructure expenses will normally be classified as Fixed Equipment and allocated under Building Depreciation in IHE F&A proposals. For IHE proposals not using the simplified method, these costs should be allocated on an FTE basis as opposed to a square footage basis. The foundation for this position is that 'users' are a more appropriate allocation basis than 'square footage' for the use of a Wi-Fi system. In addition, the use of Wi-Fi by students must be considered. Therefore, an appropriate allocation methodology to use for IHE Wi-Fi information technology system infrastructure costs is the same allocation methodology that is used for the Library cost allocation, or a similar allocation.

STEPS

COMMENTS

15. Determine if the pools include costs resulting from FASB 143 and FIN 47, Accounting for Conditional Asset Retirement Obligations (See Bulletin).

The increase in depreciation expense related to FASB 143 is unallowable because the depreciation costs cannot exceed the acquisition costs of the asset and this is an estimated liability that is not part of the acquisition cost of the asset. The negotiator should review that institutions do not include the additional depreciation based on the asset retirement obligation unless the university sets up a trustee account (similar to retirement) by building and funds it based on an actuarial determination, amortizing the unfunded liability with the stipulation that any unused Federal balance revert back to the Federal government.

16. Determine that the depreciable lives that have been established are reasonable and supported by historical data.

Guidance in this area can be found in the Cost Principles 2 CFR part 200.436(d)(1).

Note: See the Section VI. Space, for guidelines for review of allocation methods applicable to all space-related costs, including Depreciation.

IV. INTEREST

Interest expense paid to external third parties where there is an arms length transaction is allowable when associated with (1) buildings acquired or completed on or after July 1, 1982, (2) major reconstruction and remodeling of existing buildings completed on or after July 1, 1982, and (3) acquisition or fabrication of capital equipment costing \$10,000 or more. The assets must be used in support of sponsored agreements and the total cost including depreciation, operations and maintenance costs and interest should not exceed the rental cost of comparable assets in the same locality. The interest expense is allocated in the same manner as the depreciation on buildings, equipment and capital improvements to which the interest relates.

When a proposal contains interest expense, detailed documentation concerning the financing arrangements should be requested so that an in-depth evaluation of the proposed costs can be made. The interest component of the proposed rate may be comprised of indebtedness at the state level through the issuance of general obligation bonds and/or at the university level through institutional financing arrangements. In either case, the interest expenses included in the proposal must be reconciled to the State Wide Cost Allocation Plan or to the university general ledgers, respectively. All interest must be assigned specifically to a reconstruction or remodeling project, a building acquisition or construction, or an acquisition or fabrication of capital equipment costing \$10,000 or more.

STEPS

1. Verify actual interest payments and reconcile to audited financial statements.

Are there any proposed interest costs which are not included in the audited financial statements?

COMMENTS

A state college or university will frequently claim interest expense incurred through the issuance of State general obligation bonds (GOB). This GOB interest expense is usually recorded at the State level and therefore is not included in the university financial records. All GOB interest included in the F&A rate proposal must be part of an approved Statewide Cost Allocation Plan. This can be verified with the respective CAS Branch Chief for State and Local Governments. If the interest expense was not approved as part of the State Wide Cost Allocation Plan, then the CAS should eliminate the proposed GOB interest expense from the F&A rate

STEPS

COMMENTS

proposal. If the CAS office has not yet approved the Statewide Cost Allocation Plan, verify that the amount in the proposal is the same as the amount proposed in the Statewide Cost Allocation Plan. A condition may be made in the negotiation letter that this cost is subject to final approval.

Some universities propose both GOB interest and institutional operations interest. Regardless of the type of interest incurred, the institution is responsible for identifying the interest expense to individual projects. Either the State or the University System or other administrative component must assign GOB interest expenses or university interest expense to individual capital projects and buildings.

STEPS

2. Obtain the financing agreement including the prospectus, schedule of loan payments etc.

COMMENTS

This agreement should contain the amount and purpose of the loan; as well as the applicable interest rate(s), term of the loan, the lender and the maturity schedule.

For State universities, funds are allocated to universities through legislative action. Documentation to support this can be requested from the university.

Determine if the term of the loan is consistent with the proposed useful life of the asset. For instance, it would not be appropriate to pay interest over a twenty (20) year period for an item of equipment with a useful life of only ten (10) years.

The Cost Principles state that interest attributable to fully depreciated assets is unallowable. Interest expense incurred due to financing terms that exceed the depreciable life of an asset should be adjusted downward to reflect the interest expense that would be allowable if the financing term was equal to or less than the life of the asset. For interest associated with buildings that have been componentized, the interest should be allocated to the three primary component categories. The allowable interest should then be the lesser of the interest that would result from the amortization of the loan over the different component useful lives or the interest that is being incurred over the current financing term.

It would also not be appropriate to use the term of

STEPS

COMMENTS

financing as the estimated useful life of the asset if the useful life is actually longer than the terms of financing.

Interest-only debt financing may not be equitable to the Federal government. This is inconsistent with the intent of the cost principles where interest is paid on a declining principle balance theory. Interest-only loans result in excessive interest payments because the principle loan balance does not decrease over the life of the loan. This will be analyzed on a case-by-case basis.

Determine if the lender is an external, independent third party.

Determine if the current loan is merely a method for retiring old debt referred to as defeasance. Interest associated with refinancing or retiring older debts is not allowable. Interest associated with increasing the size of a loan on an asset originally constructed or acquired on or after June 30, 1982, is also not allowable. In both of these cases, the interest is not related to the acquisition or construction of the asset and is therefore unallowable.

STEPS

COMMENTS

3. Evaluate the computation of interest expense.

The institution must provide detailed information supporting its computation of the proposed annual interest expense.

The interest expenses associated with each building or construction project must be provided with the F&A rate proposal. In addition, the proposed interest expense must reconcile to a maturity schedule. This information should be submitted with the F&A rate proposal. If it is not submitted, the negotiator should request the information from the institution. The University is required to maintain and track the term of the loan and maturity schedules.

4. Determine the percent of financing for the acquisition of a building or renovation of an existing facility.

For debt arrangements over \$1 million, a reduction of interest expense is required unless the institution makes an initial equity contribution to the asset purchase of 25 percent or more. The reduction will be an amount equal to imputed interest earnings on excess cash flow.

5. Verify proposed capitalized interest cost of each building.

The institution should clearly identify the amount of capitalized interest associated with each building. Evaluate the accuracy of the proposed amounts. This may include reconciliation and verification to financing

STEPS

6. Determine how much of the proposed purchase or construction cost is associated with the building versus the land. Verify that the basis for making the split is reasonable.
7. Where appropriate, a lease vs. purchase analysis may be necessary to determine the most economical approach.

COMMENTS

agreements and building contracts.

An independent appraisal should have been performed to establish the cost of the land versus the building. When was the appraisal performed? How does the appraisal relate to the construction activity? For example, did the institution purchase an old uninhabitable building for its location or availability with the sole purpose of gutting and renovating the interior? In this case, it may be more appropriate to assign the purchase costs as land since the intent was to purchase the land and a building shell.

Federal reimbursement should be limited to the least costly alternative based on the total cost analysis.

V. OPERATION AND MAINTENANCE (O&M) EXPENSES

The expenses under this heading are incurred for the administration, supervision, operation, maintenance, preservation, and protection of the institution's physical plant. They include expenses such as janitorial and utility services repairs and ordinary or normal alterations of buildings, furniture and equipment; care of grounds; maintenance and operation of buildings and other plant facilities; security; earthquake and disaster preparedness; environmental safety; hazardous waste disposal; property, liability and all other insurance relating to property; space and capital leasing; facility planning and management; and central receiving. The operations and maintenance expense category should also include its allocable share of fringe benefit costs, depreciation and use allowances, and interest costs, in accordance with Appendix III Section B.4. of the Cost Principles. Operations and maintenance costs are allocated in the same manner as depreciation.

STEPS

1. Obtain the following documents:
 - a. A detailed breakout of O&M expenses by sub-pool if applicable, including a summary of any direct charging (recharging) of O&M expenses.
 - b. Allocation statistics for each O&M sub-pool.
 - c. A map identifying the location of utility meters and a list of utility meters at the institution.
 - d. University capitalization policies.
 - e. University telephone directory.

COMMENTS

Many universities expense costly capital construction projects, such as roof replacements, new heating, ventilation and air-conditioning (HVAC) systems, road construction, boiler replacement etc. Non-capitalized expenditures, capital construction, renovation, alteration, equipment and similar accounts should be analyzed to assure the university is adhering to its' capitalization policies. Appropriate adjustments should be made for those costs that were expensed rather than capitalized in accordance with their capitalization policies. Be alert during the review to determine how ancillary costs to the main project costs are treated. Some institutions separate project costs into different components to keep the overall project costs under the established institutional capitalization level. For example, an institution with a \$75,000 capitalization level may choose to account separately for the actual

STEPS

COMMENTS

- costs of a new boiler (\$70,000), the costs for shipping and delivery (\$5,000) the installation costs (\$20,000) and the costs for peripheral hardware and setup (\$10,000). In this case the total cost would be \$105,000 and it should be capitalized rather than expensed.
- The negotiator should determine whether the IHE complies with their capitalization criteria contained in the IHE's accounting policies and with the Cost Principles.
2. Analyze the O&M pool.
- a. Analyze the reconciliation of the proposed O&M pool to the audited financial statements.
- b. Ensure that applicable credits have been made to the pool.
- Institutions may receive insurance premium rebates and recoveries related to the physical plant. These rebates and recoveries should be credited to the O&M cost pool. A review of the miscellaneous income accounts may reveal these items.
- c. Changes in cost accounting practices.
- The negotiator should review the O&M pool to ensure compliance with the Cost Principles definition of O&M costs. If the institution changes their costing accounting practices used in the previous proposal to conform to the Cost Principles definition of O&M costs, a further justification of the change is not necessary. However, changes in cost accounting practices that

STEPS

- d. Determine if the IHE is proposing a Utility Cost Adjustment (UCA).
- e. Review the metering study to ensure that the metering was completed for the full year.
- f. Review departmental or department paid O&M, if applicable.
 - 1. Obtain a detailed listing of proposed departmental O&M costs by object code or sub-account code
 - 2. Obtain a detailed listing of departmental O&M charges to sponsored projects by object code or sub-account code.
 - 3. Determine whether the same object codes or sub-account codes are being charged indirect and direct.

COMMENTS

may involve a shifting of costs from a capped pool to an uncapped pool should be disclosed by the institution and be analyzed by the negotiator.

All IHE preparing a Long-Form F&A rate proposal are eligible to propose a Utility Cost Adjustment (UCA). For details see the section following this O&M section regarding the UCA.

It is unacceptable for a university to meter for a selected period of time and project the costs for the year.

Many institutions are reclassifying directly charged non routine repair and maintenance costs back to the O&M cost pool.

In many instances, the non-routine repair and maintenance costs that are charged to academic departments are directly charged to Federal sponsored projects. Similar costs that have not been charged to Federally sponsored projects are classified back to an O&M sub-pool titled departmental O&M and subsequently allocated to department functions based on space assigned to each function. This practice results in a CAS 502 violation. When a departmental O&M cost pool is proposed, the negotiator should request a schedule that lists the object or sub-account codes that are charged to academic departments. The

STEPS

COMMENTS

g. Examine any recharging of O&M costs.

schedule should show the total cost for each object or sub-account code and the amounts charged directly to Federal sponsored accounts, non-Federal sponsored accounts and unrestricted accounts. Depending on the materiality of charges to Federal accounts, an adjustment may have to be made to compensate for the inconsistent costing.

Certain institutional functions such as auxiliary enterprises, hospitals, bookstores, etc., may be direct charged for O&M costs through a recharge mechanism. These charges and the recharge mechanism should be reviewed to ensure that the charges are based on actual costs, are consistently applied and appear fair and equitable. It is particularly important that these functions pay for the full amount of O&M costs (including administrative costs) that they use, so that they are not subsidized by other functions, including organized research.

h. If there is more than one O&M pool, determine if the allocation base for each pool is reasonable.

Institutions are increasing the number of O&M sub-pools which usually results in an increase of O&M costs allocated to organized research. Numerous O&M sub-pools may indicate a higher risk and therefore a more intense review and analysis is necessary. This is a form of "cherry picking" the O&M cost categories.

STEPS

COMMENTS

Each sub-pool should be reviewed to determine if the types of costs recorded in the accounts that are assigned to the sub-pool are appropriate when looking at the allocation base used to distribute these sub-pooled costs. O&M sub-pools should be allocated to all benefiting activities.

For example, separate O&M sub-pools may be created for the campus environmental health and safety unit and the campus police force. The negotiator should ensure that an equitable allocation base is used for each sub-pool. For example, an institution may attempt to allocate 100% of the campus environmental health and safety costs to research laboratories claiming that they are organized research costs. These costs, at a minimum, should be allocated to both classroom laboratories (teaching) and research laboratories. An analysis of the costs in the pool and the activity performed will provide a clearer picture how to more appropriately allocate the costs.

In addition, the campus police may provide significant effort at athletic events, concerts, other student activities and general night-time safety for students.

Consequently, it may be more appropriate to allocate the costs of the campus police on some basis that reflects effort, such as FTEs, rather than using the normal square footage allocation.

STEPS

- i. Determine if O&M costs were allocated based on overall square footage of university buildings rather than building by building. If so, is there a more precise allocation base for certain O&M components and is the appropriate data available?

COMMENTS

Once the university establishes separate O&M sub-pools for what they consider more appropriate allocations to organized research, the negotiator should consider reviewing the activities included in the general O&M pool to identify activities that could be over allocated to organized research using square footage statistics.

UTILITY COST ADJUSTMENT

In the December 2013 release of 2 CFR part 200, in Appendix III B.4.c., provisions were added to extend to all IHEs the provisions previously extended only to the 66 IHEs listed in Exhibit B of the OMB Circular A-21. These provisions allow for recovery of increased utility costs associated with research by computing a utility cost adjustment (UCA). This UCA is subject to review and may be included in the negotiated indirect cost rate of the IHE for organized research. The UCA is developed using the computation alternatives contained in the Cost Principles, in Appendix III B.4.c.(1) and (2). The UCA uses a relative energy utilization index (REUI) which is provided on the OMB website.

The amount recoverable for the UCA is limited to an amount equal to 1.3 percentage points of the IHE's indirect cost rate. A lower rate amount may be negotiated based on adjustments to the proposed UCA and/or due to a UCA calculation by the IHE of less than 1.3 percentage points.

STEPS

1. Review the UCA proposal for accuracy and adherence to the Cost Principles and to the Frequently Asked Questions (FAQ) presented by the COFAR on OMB's Uniform Guidance at 2 CFR 200 published in September 2015.

COMMENTS

The UCA computation should be a separate proposal provided as a supplement to the actual cost proposal. If the IHE's actual cost proposal implements the UCA computation, it must be returned and resubmitted without the UCA inclusion. The actual cost proposal utility allocations should be no different than prior proposals. For example, utility costs should not use "effective square footage" as defined by the Cost Principles in the actual cost proposal. In addition, utility costs still may not be allocated on a basis finer than the building level. The negotiator should determine if the

STEPS

2. Review the UCA rate schedules to ensure that the UCA was not included in the rate(s) other than the research rate.
3. Determine whether the IHE was one of the 66 IHEs listed in Exhibit B of the OMB Circular A-21 that were receiving a 1.3% UCA.

COMMENTS

IHE is potentially violating the intent of the UCA by having more than one meter per utility per building. With multiple meters per building, there is the potential of research receiving an excessive allocation of utility costs. Related to this issue, review the buildings to determine if the university has divided a building into multiple units so as to increase the metering and therefore the costs allocated to research.

Universities should not receive the UCA for rates other than the organized research rate.

For IHE's that received the 1.3% UCA under the OMB A-21 Circular (prior to the new 2 CFR part 200), these IHE's will not lose the automatic 1.3% until the negotiation of their next submitted proposal for the base years 2016 and beyond. Base year proposals for 2016 and forward must propose the UCA using the UCA computation in the current Cost Principles. This computation is not required for base year proposals 2015 or earlier for these IHE's.

IHE's not currently receiving the UCA may begin proposing the UCA in accordance with section B.4.c of Appendix III with base year 2014 proposals and forward, subject to negotiation.

STEPS

4. In the IHE's UCA calculations, determine if any buildings have space identified as a single function and that space is separately metered per the Cost Principles, in Appendix III B.4.c.(1).

5. Determine that the proper laboratory space was used in the UCA computation and that the REUI was properly applied to all functions within that laboratory space.

COMMENTS

If in the UCA computation a building uses sub-metering for the single function space then that same building may not use the "Effective Square Footage" (ESF) calculation. Any buildings using this single function methodology in the UCA computation becomes part of the UCA add-on which in total is subject to a cap of 1.3%. In the actual cost proposal IHEs may not sub-meter and allocate utility costs at a level finer than the building level. The single function methodology may only be used in the supplemental UCA proposal. Also please note, Organized Research is not applicable as a single function space because space at IHEs should not be coded 100% Organized Research due to other activities sharing the space such as Instruction and Departmental Research.

The type of labs that may receive the REUI are: Fume-hood intensive biological, chemistry, and life sciences labs; and physical labs that have high plug loads due to an abundance and variety of electrically-powered instruments; and other labs requiring 100% outside air. The majority of the labs included in the lab energy index are chemical and biological labs. The major driver of the lab energy index is the air exchange requirement. Laboratories typically require 100% outside air for ventilation at higher rates than other commercial buildings.

Research offices, office-type desk-based research

STEPS

COMMENTS

rooms that are similar to administrative offices with a typical laptop or desktop computer on each desk, and greenhouses should not have the lab REUI applied. The only exception would be if the Institution can demonstrate these other room types require 100% outside air for ventilation at rates similar to biological and chemical labs, or otherwise have the characteristics of the lab facilities included in the lab energy index.

All activities/functions (Research, Instruction, OSA, etc.) within those laboratories receiving the application of the REUI must be considered in calculating the “effective square footage”.

A UCA Calculation Example provided below:

UCA Calculation Model

Step 1: Breakout Utility/Utility-Related Costs by Building

Step 2: Allocation of Building #1 - Utility/Utility-Related Costs based on Space Study SF (current methodology)

Building #1 Utility Costs	Room Type Category	ASF	% Total ASF	Allocation Based on OR SF	
\$4,000,000	Labs / Lab Services (OR)	40	40.0%	\$ 1,600,000	
	Labs / Lab Services (Non OR)	10	10.0%		
	Offices (OR)	20	20.0%	\$ 800,000	
	Offices (Non OR)	25	25.0%		
	Others (Non OR)	5	5.0%		
		<u>100</u>	<u>100.0%</u>	<u>\$ 2,400,000</u>	(A)

Step 3: Allocation Based on UCA Methodology

REUI Factor 2

Building #1 Utility Costs	Room Type Category	ASF	Adjusted ASF for UCA *	% Total UCA ASF	Allocation Based on OR SF	
\$4,000,000	Labs / Lab Services (OR)	40	80	53.3%	\$ 2,133,333	
	Labs / Lab Services (Non OR)	10	20	13.3%		
	Offices (OR)	20	20	13.3%	\$ 533,333	
	Offices (Non OR)	25	25	16.7%		
	Others (Non OR)	5	5	3.3%		
		<u>100</u>	<u>150</u>	<u>100.0%</u>	<u>\$ 2,666,667</u>	(B)
Difference					\$ 266,667	(B) -(A)

Step 4: Comparison of OR F&A Rate (OR F&A Rate Calculated based on A vs. B)

- a. Determine the difference between (A) and (B)
- b. Calculate the sum of the differences for each of the buildings
- c. Divide the total difference by the Organized Research MTDC Base used for O&M; = UCA
- d. - If the UCA is > 1.3 points, then add 1.3 to the proposed F&A rate.
 - If the UCA is < 1.3 points, then add the calculated UCA to the proposed F&A rate.

* 2 times ASF in Lab/Lab Services

VI. SPACE

Understanding how an IHE assigns space to functional activities (organized research, instruction, other sponsored activities, and other institutional activities) through a space use survey is one of the key aspects of the proposal review. The importance of this space assignment is based on the fact that facility costs including building and equipment depreciation, improvements to land, capital interest and interest associated with loans on buildings used for organized research, and operation & maintenance costs are allocated to institutional functions based on use of space. The most common method for assigning space to a function is to conduct a space use survey. The survey should have been coordinated university wide with adequate written instructions, policies and procedures. Training should have been provided to all individuals responsible for performing the actual survey. The responsible persons should be familiar with the Cost Principles' academic functional definitions, have knowledge of a department's space and its occupants and have knowledge of the funding sources for the room occupants. The negotiator should verify this information by interviewing selected department representatives or other individuals responsible for performing the survey. The survey should have been performed room by room for certain room types when a space use survey is conducted. Under this space use survey method, the percentage of salaries & wages incurred for each function in a department may not correlate with the space allocated to each function. Consequently, the space survey needs to be reviewed thoroughly to determine its accuracy. Assignment of space based on predominant use is not acceptable.

The default methodology prescribed in the Cost Principles require that space related costs be allocated using a salary and wage or full time equivalent (FTE) basis. This is the same methodology that the Cost Principles prescribe to allocate jointly used space.

STEPS

COMMENTS

1. Obtain the following documents:
 - a. Space use survey instructions, survey forms, functional definitions, and survey policies and procedures.

STEPS

COMMENTS

include departmental research and thesis research performed by students unless the student is paid by an organized research project for the thesis work.

STEPS

- c. Determine if the functionalized space assigned to organized research is consistent with the MTDC base costs assigned to organized research. When rooms are coded to organized research, the university must also identify both sponsored and non sponsored accounts that fund the organized research in the room.

COMMENTS

The negotiator must be assured that the university's space use survey accurately assigns space to functions; and the assignment is consistent with the MTDC base costs assigned to the same function. It is important to remember that when a university codes rooms as organized research, then both sponsored and non sponsored accounts used to fund the organized research in that room also be identified.

When developing the MTDC rate base for organized research, the institution will often reclassify accounts from the financial statement organized research classification to instruction and departmental research. In this situation, the negotiator must first assure that the reclassification is appropriate. If the reclassification is not appropriate, then the negotiator should move the reclassified accounts back to the organized research MTDC base. If the reclassification is appropriate, then the negotiator needs to confirm that the reclassified accounts were not used to classify space in support of organized research. This can usually be accomplished by having the departments identify the room or rooms in which the reclassified account dollars were utilized and then looking at how the room's space was functionalized. This information may be readily available if the university performed the survey using a web-based space survey system. As discussed in the Section II. c., Step #5, research training grants can be classified as either organized research or instruction as

STEPS

COMMENTS

long as the related space is consistently assigned. Also, as indicated in Step #4 of that Section, cost shared research effort and the space where the effort is performed must be treated consistently.

Where the university chooses certain room types to allocate space costs using salaries and wages or FTE, the negotiator should verify that the numbers used were appropriate. When using salaries and wages, it may be necessary to impute salaries and wages for clinical, institutional faculty, postdoctoral fellows, visiting professors, graduate students or other room occupants who are not on the university payroll. Imputed salaries and wages should be assigned to the appropriate function depending on the nature of the effort. When an institution classifies space as organized research using imputed salaries and wages, then the imputed salaries and wages and associated fringe benefits must be added to the organized research direct cost base.

d. Review the treatment of space assigned to a single function.

Single function space, where identified, must be assigned to that function. This would normally include buildings and space associated with student housing, general administrative activities, auditoriums, classrooms, other institutional activities, etc.

e. Review the treatment of Joint Use Space.

The negotiator should verify that all activities that use joint use space receive an allocation of associated space costs. Activities which may have been excluded could include patient care, student services and other

STEPS

COMMENTS

- f. Conduct a site visit to determine the accuracy of the space use survey.

institutional activities.

Joint use space should be allocated to the benefiting functions on the basis of:

- a. the employee FTEs or salaries and wages of those individual functions benefiting from the use of that space; or
- b. institution-wide employee FTEs or salaries and wages applicable to the benefiting Major Functions of the institution.

Any use of multiple distribution bases for joint use space should be carefully evaluated for compliance with the Cost Principles.

In many cases, it will be necessary to visit the university to test a sampling of rooms to determine if the rooms were functionalized properly and to evaluate the reasonableness of the space use survey. In order to select the space to be reviewed, an analysis which compares departmental S&W costs to departmental space usage may be useful. This analysis may reveal discrepancies, such as a situation where a department has a relatively small percentage of salary & wage costs charged to research, but a high percentage of space charged to research. Such discrepancies should be investigated. Also, it is useful to compute the ratio of research assignable square feet to research salaries in

STEPS

COMMENTS

a department. A high ratio (e.g., high amount of space per salary dollar) may indicate misclassified space.

When evaluating the space sampled, the current user of the space (such as the principal investigator) or a person knowledgeable about the use of the space, the occupants of the space, and the direct cost funding for the space should be interviewed to verify the accuracy of the space usage per the survey. It may also be useful to compare the usage per the survey to the payroll records or Personnel Activity Reports (PAR) forms of the persons using the space in order to determine if these are consistent. Significant inconsistencies could lead to questioning the validity of the space survey.

SPECIAL NOTE: The negotiator should be permitted to conduct an independent review of the space survey. University representatives may accompany the negotiator as appropriate. If the negotiator feels that they are being intimidated and constantly interrupted for asking questions regarding the methodology used to assign the functions to rooms, the negotiator may stop the space validation and the survey will be considered unacceptable. The facility costs will then be allocated using the default methodology prescribed in the Cost Principles requiring that the facility related costs be allocated using a salary and wage or full time equivalent (FTE) basis.

STEPS

COMMENTS

Space under construction should **not** be reported as usable space and included in the space use survey. See Section XII.J. titled facility cost projections.

ALTERNATE SPACE METHODOLOGY

The purpose of this section is to provide IHE guidance on an alternate method intended to streamline the effort and reduce the cost incurred in performing space surveys. It is critical to note that this alternate method does not reduce the importance of performing an accurate and well-documented space survey. Institutions employing this alternate method will be held to strict standards. Institutions failing to provide accurate and fully supported space surveys, whether using this method or performing a complete space survey, will be subject to having all space related costs re-allocated using department salaries and wages or FTE.

An institution choosing this alternate method would establish an Organized Research modified total direct cost (MTDC) dollar threshold to determine which academic departments and/or schools are to be surveyed. Once an MTDC threshold has been determined, academic departments/schools that fall under the established threshold must allocate their space using departmental salaries and wages, including imputed salaries where appropriate, or FTE. For example, an institution may choose to survey all academic departments where Organized Research MTDC is equal to or exceeds \$400,000. This alternate method would require that all academic departments/schools with less than \$400,000 of Organized Research MTDC allocate their space using departmental salaries and wages, including imputed salaries where appropriate, or FTE. Academic departments/schools over the established dollar threshold must be surveyed and use the room type allocation methodology described below.

The following alternate methodology allows an institution to survey certain room types, employ joint use for other room types and assign some room types 100% to a specific function. The institution cannot apply different methodologies to the same room type. For example, if an institution chooses to survey research laboratories, then all research labs in academic departments/schools over the university dollar threshold must be surveyed. If an institution chooses to allocate faculty offices using salaries and wages, then all faculty offices in academic departments/schools over the university dollar threshold must be allocated using salaries and wages.

<u>ROOM TYPE</u>	<u>ALLOCATION BASIS</u>	<u>COMMENTS</u>
1. Research Laboratories	Space Survey	<p data-bbox="1346 375 1944 586">A main research laboratory would be defined as the primary research laboratories assigned to a principal investigator where researchers have space available to use for conducting organized research.</p> <p data-bbox="1346 634 1944 1065">As described in the preceding section, all room occupants must be taken into consideration when surveying room use, whether they are paid or not. This includes visiting professors, professor emeriti, clinicians, undergraduate or graduate students, high school students for educational events, etc. Space must also be assigned to room occupants who are supported by costs that may have been excluded from the MTDC functional bases such as stipends.</p> <p data-bbox="1346 1114 1944 1398">All space that is classified as organized research must be supported with organized research accounts, gift accounts, university accounts or other accounts from which the room occupants are paid. Imputing salary for occupants not paid by the institution may be appropriate.</p>

<u>ROOM TYPE</u>	<u>ALLOCATION BASIS</u>	<u>COMMENTS</u>
2. Research Laboratory Service / Shared Labs. This may include cold rooms, microscope rooms, culture rooms, dark rooms, shared equipment rooms, researcher computer rooms, research supply storage rooms, etc.	Use the average percentage of functional use for all the research laboratories that share these types of rooms. The institution needs to document what rooms were used in calculating the average.	<p>Any adjustments applicable to the research laboratories would also apply to this space.</p> <p>If all the research laboratories in the academic department or the building share this space, then the space should be allocated using an aggregate average of all the research laboratories in the academic department or the building, respectively.</p> <p>Consideration must also be given to other users who are not using the research laboratories but are using research laboratory service / shared Laboratory rooms.</p>

<u>ROOM TYPE</u>	<u>ALLOCATION BASIS</u>	<u>COMMENTS</u>
3. Class Laboratory, Class Laboratory Service, Classrooms, Classroom Service, Departmental Classroom, Departmental Classroom Service, Departmental-only Research, Study Room, Study Service, Graduate Assistant Office/Student Offices, Student Computer Rooms, etc.	100% to Instruction	This direct allocation will simplify the overall space survey process.
4. Departmental Administrative Offices, Departmental Administrative Storage Rooms, Data Processing, File Rooms, Copy Rooms, Break Rooms, Auditoriums, etc.	Departmental Salaries & Wages including imputed salaries where appropriate or FTE.	Salaries not received from the institution or not included in the department's salaries and wages for occupants using these rooms must be included in the allocation base. Examples would include clinical salaries, visiting professors, professor emeriti etc. This would include imputed salaries where appropriate.
5. Faculty Offices, Departmental Conference Rooms and Libraries	Departmental Salaries & Wages including imputed salaries where appropriate or FTE.	Salaries not received from the institution or not included in the department's salaries and wages for occupants using these rooms must be included in the allocation base. Examples would include clinical salaries, visiting professors, professor emeriti etc. This would include imputed salaries where appropriate.

<u>ROOM TYPE</u>	<u>ALLOCATION BASIS</u>	<u>COMMENTS</u>
6. Utility Rooms, Cleaning Closets and Maintenance Storage, etc.	Operations and Maintenance or Non-Assignable Area	
7. Specialized Service Facilities (SSF)	Specialized service facilities (SSF) should include the facility costs in their billings rates. Where an institution includes facility costs in calculating their SSF billing rates, the SSF is identified as a separate functional cost objective. If an institution chooses not to include the facility costs in the billing rates, then the applicable facility costs must be assigned to other institutional activities (OIA). In either case, the space assigned to the SSF shall be used as the allocation basis.	For treatment of Animal Research Facilities see the subsection Special Requirements for Animal Research Facilities (ARF) included in XII B Specialized Service Facilities (SSF).

<u>ROOM TYPE</u>	<u>ALLOCATION BASIS</u>	<u>COMMENTS</u>
8. Recharge Centers	For recharge centers that are not required to be treated as specialized service facilities, the facility costs may be assigned to functions based on revenue generated from the users.	All users must be considered, whether they are billed or not. Imputed revenue needs to be added where services are provided to some users without charge or at a reduced charge. Where an institution includes facility costs in calculating their recharge center billing rates, the recharge center shall be identified as a separate functional cost objective or OIA, and the space assigned to the recharge center shall be used as the allocation basis.
9. Vacant Space (Idle facilities)	OIA (or) Departmental Salaries & Wages including imputed salaries where appropriate or FTE, depending on the nature of the space and the length of time it is expected to be vacant.	As defined by 2 CFR part 200.446 of the Cost Principles, if the related space is determined to be unallowable, then classify the space as OIA. If the related space is allowable, then allocate space on departmental salaries and wages including imputed salaries where appropriate or FTE.

VII. LIBRARY EXPENSES

Library expenses are the costs incurred for operating the library including the cost of books and library materials less appropriate applicable credits. Library expenses shall be allocated to institutional functions using the users of library services including students, professional employees and other users. Each user category shall be calculated on a full-time equivalent basis. The costs allocated to the student category shall be assigned 100 percent to the instruction function. The costs allocated to the professional employee category shall be assigned to the major functions of the institution in proportion to the salaries and wages of faculty and professional employees. The costs allocated to all other users shall be assigned to the "other institutional activities" function.

The library environment has changed considerably over the years due to the increased use of online library services which continues to grow significantly. Since there may be an increase in the amount of outside users, additional analysis may be required for the amount of expenditures allocable to other institutional activities.

STEPS

1. Reconcile claimed expenses to the financial statements.

COMMENTS

Certain activities such as the audio-visual learning center and computer assisted instruction should normally be directly assigned to instruction. Determine if these services are included as part of library operations. These activities may be treated as recharge centers and direct charged to users.

The costs for rare book purchases as well as museum and exhibit centers should be excluded from the allocation process and assigned to OIA.

STEPS

COMMENTS

2. Determine if the university has separate libraries that serve specific areas of knowledge such as a health sciences or medical library, a law library or engineering library. If the operating costs are material, the university may choose to allocate these costs separately from the main library. This may only be considered when a library user study is performed. If a library user study is not performed, then all libraries must be allocated using the standard allocation method prescribed in the Cost Principles.
3. The university should provide schedules to support the full-time equivalent (FTE) numbers including a complete explanation of the methodology used to calculate the FTEs by category and the source of the information.

Appropriate adjustments should also be made for the income received from online services, fines, penalties, other fees and from library sales such as copy center services, fax services, etc.

Most medical universities have a separate health sciences or medical library to service medical school faculty and students and affiliated hospitals. Affiliation agreements between the university and the affiliated hospital should be reviewed to determine if there is any reimbursement for library usage and how it is determined.

The negotiator should review the FTE computations to assure that the FTE numbers were determined using a fair and reasonable method. Verify whether voluntary and visiting faculty members are included in the FTE count and that the salaries and wages are imputed for inclusion in the S&W allocation base. Health science complexes (Hospital/Medical School) have voluntary faculty that teach courses in return for admitting privileges at owned or related hospitals.

Many universities offer continuing education classes (non-credit classes, etc.) to the general public and students. These individuals and other outside users including university alumni, friends of the library, guests and community professionals as appropriate must be

STEPS

COMMENTS

4. Costs should be assigned to the following categories:

a. Professional employees include faculty members and other professional employees. This category may also include postdoctoral fellows and graduate students being paid. Administrative employees are excluded from this category. The cost allocated to the professional employee category is further distributed to all the major functions of the university based on the salaries and wages applicable to those functions.

The salary and wage amounts associated with the major functions should be reconciled to the appropriate records.

b. Students include all individuals enrolled as students regardless of whether they earn credit toward a degree or certificate. This information should be obtained from the registrar's office, which maintains census reports. The cost allocated to the student category is further distributed 100 percent to instruction.

c. Other users include the general public and other non university users. This category is assigned entirely to "other institutional

identified and included in the FTE count.

Students may be counted as students and as employees. The employee FTE should be based on the ratio of student employment hours to a full-time schedule.

The other user category includes all users not included in the professional employees and student category, such as the general public, university alumni and

STEPS

activities".

COMMENTS

friends of the library, guests, high school students, students and faculty from other colleges, medical professionals, and community professionals as appropriate. Assistance may be requested from the institution librarian in developing an FTE for outside users. A formula approach may be considered. The calculation of the allocation percentage for this category should be developed and evaluated on a case by case basis.

SPECIAL LIBRARY USER STUDIES

The Cost Principles require that library expenses be allocated to functions based on primary users of the library services, including professional employees, students, and other users. Some institutions perform library user studies in an attempt to determine the actual users of the library as well as the library services they use including circulation, cataloging and binding, periodicals and subscriptions, reference, on-line access and inter-library loan services. Separate statistics for each type of service used and the reason for using the service are accumulated during the user study and are used to allocate the appropriate costs. The study itself surveys everyone entering the library at a pre-selected time. Each survey time is usually determined through a statistical sample.

Library cost studies that use intended usage or cause for purchases as an allocation methodology for technical services costs, including book and periodical acquisitions, are not acceptable.

STEPS

COMMENTS

1. Obtain a copy of the library cost study, including the study methodology, survey forms, statistical sampling plan and statistical projections, and the supporting work papers.

STEPS

2. Analyze and determine the appropriateness of the library study methodology for at least the following areas:
 - a. Organization structure and cost centers
 - b. Functional definitions used in the survey
 - c. Time period covered by the study
 - d. Treatment of non-responses
 - e. Audit trail
 - f. Non-library service users
 - g. Surrogate users

COMMENTS

Library organizational charts should be used to help determine the primary library functional activities and corresponding cost centers. If the major functions do not correspond to the organizational chart, interviews with appropriate library officials, or staff surveys, may be necessary to determine the cost associated with each major library function. Depending on the materiality of the costs and the organization structure of the library, separate cost centers should be broken out in the study. Those cost centers might include library administration, reference, circulation, audio visual services, cataloging and binding, periodicals and subscriptions, inter-library loan services and on-line access.

STEPS

COMMENTS

3. Review the survey forms. Determine if the form is clear and concise, if all library functions and activities are identified and if the functional definitions are clearly explained and consistent with the functional definitions in the Cost Principles.

The cost of each of these aforementioned functions should be allocated individually based on the results of the library user survey. The study methodology should adequately substantiate and define major library functions.

Be sure that library service centers such as copy and fax centers are identified and assigned appropriate indirect costs.

The survey may identify individuals who use the library facility to study, meet other individuals, rest, and for a variety of other non library activities. These individuals do not use library services; rather, they only utilize library space. It may be appropriate and equitable to allocate library O&M costs and other library indirect costs to these individuals.

The Cost Principle definitions and terminology should be fully explained, especially the definitions of organized research and departmental research. This is critical since the individuals completing the survey forms generally do not understand the difference between "organized research" and "research" related to course assignments, thesis requirements, etc. Inadequate or unclear definitions of these terms can seriously jeopardize the validity of the study.

STEPS

4. Determine that survey forms allow for rotating the positions of the various functions to be selected.
5. Determine that the survey form includes a space for entering an identification number. Also, does the survey ask if the user is in the library for his/her own benefit or for someone else's (surrogate user).
6. Evaluate the statistical sampling methodology developed by the university to select survey periods and to project the results of users based on the results of the surveys conducted. Determine if the sampling methodology is statistically valid.
7. Determine if the survey periods selected were randomly generated.

COMMENTS

If the survey form always shows the same function (organized research) first, it may skew the survey results.

The survey should allow for subsequent review and analysis, or an audit trail. The survey form must identify the individual surveyed by a unique identification number such as social security number, university payroll number, student or employee number etc.

The survey methodology should address how surrogate users are counted versus non-surrogate users.

Assistance may be obtained from the OIG to help determine the statistical validity of the sample. Outside consultants may also be retained by the Department to assist negotiators in a limited number of cases.

Library user surveys must be conducted over a twelve (12) month period. Survey forms must be distributed to all persons entering the library during the randomly scheduled survey periods.

The survey methodology should establish acceptable response levels.

STEPS

8. Determine whether the statistical sampling plan considers weighing the usage of library services based on the number of books and periodicals used by each library user. For example, if linear weighing factors were used, an individual using two books would be assigned twice the amount of library costs as an individual using just one book.

COMMENTS

The validity of linear weighting has never been accepted as part of a valid library user study.

STEPS

9. Obtain the following information for each library surveyed and analyze the results of the surveys and the projections that are based on the results:
 - (a) mean usage, number of respondents associated with materials used in the library, materials checked out and reference services used;
 - (b) mean usage, number of items used and number of respondents assigned to each major function for materials used in the library, materials checked out and reference services used;
 - (c) mean usage, number of items used and number of respondents assigned to each major function broken-down by type of user category (e.g., faculty, staff, student, etc.)
 - (d) mean usage, number of items used and number of respondents by type assigned to each major function broken-down by materials used in the library, materials checked out and reference services used.

COMMENTS

This information should be used to help evaluate the reliability of the sampling plan and to evaluate the statistical validity of the statistical sampling method.

STEPS

10. Obtain a copy or listing of each library user survey form that indicated the library was used for research purposes. Verify that the individuals were actually working on organized research projects during the time the survey was conducted.

COMMENTS

Many individuals indicate that they are working on organized research when they are in the library; while in fact, they are not associated with organized research in any way. If this is found to be a major problem in the responses, it will be necessary to use the standard FTE allocation base.

VIII. GENERAL ADMINISTRATION AND GENERAL (G&A) EXPENSES

G&A expenses are those that have been incurred for the general executive and administrative offices of the university and those expenses of a general nature which do not relate solely to any major function of the institution. The G&A expense category may include allocated amounts of fringe benefits, depreciation, and operation and maintenance expenses. It may also include adjustments to bring in university or college system costs, Chancellor Office costs or Board of Regent costs through an approved cost allocation plan. General administration and general expenses shall not include expenses incurred within non-university-wide deans' offices, academic departments, organized research units, or similar organizational units. The G&A expenses should be grouped first according to common major functions of the institution to which they render services or provide benefits. The aggregate expenses of each group should then be allocated to serviced or benefited functions on a modified total cost base. Modified total costs consist of salaries and wages, fringe benefits, materials and supplies, services, travel and the first \$25,000 of each subaward. Equipment, capital expenditures, charges for patient care and tuition remission, rental costs, scholarships, participant support costs, and fellowships, as well as the portion of each subaward in excess of \$25,000 shall be excluded from the Modified Total Cost (MTC) base. General administration and general expenses, combined with departmental administration expenses, sponsored projects administration expenses, and student administration and services expenses, are limited to 26 % of modified total direct costs.

STEPS

COMMENTS

1. Evaluate the adequacy of the institution's reconciliation of the total G&A expense to the Institutional Support account in the audited financial statements.

STEPS

2. Obtain a list of the accounts by title and by amount that were included in the proposed G&A cost category.
3. Obtain additional information from the university on accounts which have titles that are vague or questionable.
4. Review the proposed G&A cost pool for capital expenditures and costs which are unallowable for sponsored agreements under the Cost Principles.

COMMENTS

Many institutions develop G&A sub-pools to more accurately allocate costs. Each sub-pool should be analyzed to assure the costs are properly assigned to a particular cost pool and that the distribution base is appropriate under the circumstances. There must be a correlation between the pooled costs and the distribution base.

The following expenses are some examples of unallowable costs or activities according to the Cost Principles:

- a. advertising (except costs as defined by the Cost Principles for purposes necessary to meet the requirements of a sponsored agreement or for the performance of a sponsored agreement)
- b. bad debts
- c. entertainment
- d. contributions and donations
- e. losses which could have been covered by permissible insurance
- f. fund raising
- g. investment counsel for purposes of enhancing income from investments
- h. public relations (except costs as defined by the

STEPS

COMMENTS

- Cost Principles for purposes necessary to meet the requirements of a sponsored agreement or for specific communications and liaisons considered necessary per the Cost Principles)
- i. alumni activities
 - j. news releases other than those pertaining to scientific accomplishments under sponsored agreements.
 - k. alcoholic beverages.
 - l. personal use portion of institution furnished automobiles.
 - m. contingencies.
 - n. defense against Government claims or appeals or the prosecution of claims or appeals against the Government.
 - o. patent infringement litigation.
 - p. insurance to correct defects in materials or workmanship.
 - q. fines and penalties.
 - r. goods or services for personal use.
 - s. lobbying.
 - t. membership in civic or community organizations.
 - u. memberships in country clubs, social and dining clubs.
 - v. selling and marketing costs.
 - w. malpractice insurance.
 - x. housing and personal living expenses of current and past officers.

The above costs and activities should be reviewed to

STEPS

COMMENTS

5. Review the proposed G&A expenses for costs which should be reclassified to the Student Administration and Services cost category.

determine if they should be included in the other institutional activities base and be burdened with F&A costs. All unallowable costs and activities that receive benefit from the functions in the G&A pool must be included in the modified total direct cost base.

The following costs and similar costs should be reclassified to Student Administration and Services:

- a. commencement
- b. convocation
- c. student activities
- d. student publications
- e. student clubs
- f. vice president of student services
- g. admissions and registrar
- h. counseling and placement services
- i. student accounting and billings.

6. Review cost transfers out of G&A which may represent a change in accounting or cost allocation methods.

At the time the 26% cap was placed on administrative costs, the regulations indicated institutions should not change their accounting or cost allocation methods which were in effect May 1, 1991 if the effect was to:

(1) change the charging of a type of cost from indirect to direct.

(2) reclassify costs from indirect pools covered by the cap to other indirect pools.

STEPS

COMMENTS

7. Reconcile the proposed allocation base for G&A to the total expenditures for the year. Determine what costs were excluded from the MTC base.

8. Determine if the institution has elected to use the alternative method for claiming administrative costs.

9. Confirm that G&A unallowable activities excluded from the G&A cost pools in accordance with the Cost Principles are included in the other institutional activities modified total direct cost base.

Changes may be permitted when an institution's charging practices are at variance with acceptable practices followed by a substantial majority of other institutions.

The MTC base should include all unrestricted and restricted expenses less operations and maintenance expenses, G&A expenses, tuition remissions, student support costs (such as student aid, stipends, scholarships, fellowships), participant support costs, patient care costs, capital expenditures, rental costs, alterations and renovations, and that portion of each sub-award in excess of \$25,000.

Institutions may elect to claim a fixed allowance for the Administration portion of indirect costs. The allowance could be either 24% of MTDC or a percentage equal to 95% of the most recently negotiated fixed or predetermined rate for the cost pools included under "Administration", whichever is less. Refer to the Cost Principles, Appendix III, Section C.9. for details of the calculation.

Unallowable activities such as fund raising, alumni activities, investment management etc. should be treated as part of other institutional activities and be allocated their share of G&A, O&M and any other indirect costs.

STEPS

COMMENTS

10. Determine that cross allocations are not included in the MTC allocation base.
11. Determine if G&A expenses should be assigned to university or non-university activities that are not included in the university's financial statements (e.g., medical practice plans, hospitals, insurance companies, utility companies, printing companies, real estate companies, etc.).
12. Determine the accuracy and appropriateness of allocations or billings of G&A services provided to affiliated organizations, such as hospitals. Be sure that the distribution method is a reasonable measure of services rendered.
13. Ensure that G&A expenses are grouped first according to common major functions of the institution to which they render services or provide benefit.

The standard allocation methods for departmental administration and administrative and general expenses use the term Modified Total Cost (MTC). The MTC base includes the cross allocation of the other cost pools to which the G&A expenses are allocated (e.g., libraries, student administration and services, etc.) However, the indirect costs previously allocated to those functions (such as; depreciation and operation and maintenance expenses) should be excluded.

Allocations or billings to affiliated organizations should be based on supportable allocation statistics or on the cost of the services. If the allocation or billing is not supportable, costs should be reclassified back to the G&A cost pool and the affiliate direct costs should be included in the allocation base statistics.

Review G&A expenses for those costs which do not benefit all functions of the university. Make appropriate adjustments to the allocation process.

STEPS

14. Review costs included in G&A that were made as adjustments into the pool rather than having been recorded on the institution's financial statements. Examples include costs allocated through a Statewide Cost Allocation Plan, a System-wide office cost allocation plan or a Chancellor's office or Board of Regent's cost allocation plan.

15. If applicable, review the Statewide Cost Allocation Plan, University or College System Administrative Offices, Chancellor's Office costs or a Board of Regent's costs.

COMMENTS

Certain costs may be allocated to a State college or university through an approved cost allocation plan from another segment of the State. See next step.

States, through their Statewide Cost Allocation Plans (SWCAP) will frequently allocate State central service costs to their State College and or University administrative organizations or directly to the individual campuses. Because the State central service costs are being allocated through the SWCAP, the appropriate cost principles would be 2 CFR, part 200, Appendix V. State College and or University administrative organizations may be called a University Systems Administration Office, a Chancellor's Office or a Board of Regents. Once the statewide central service costs are allocated to the administrative organizations, the administrative organizations must allocate the costs from the SWCAP, as well as their own operating costs to the various campuses under their control. This cost allocation must be based on the cost principles contained in 2 CFR, part 200, Appendix III. (Occasionally, the Board of Regents is a state Board that is not part of the University System. In this case, the Board of Regents costs may be subject to

STEPS

COMMENTS

Appendix V, and are potentially unallowable general costs of government.)

There must be an approved cost allocation plan for the administrative organization with the CAS. If a plan is not approved and on file, all administrative organization costs including the allocated Statewide costs (unless allocated directly to campuses) should be considered unallowable. If the CAS office has not yet completed the review and approval of the SWCAP, verify that the amount claimed in the F&A rate proposal is the same as the amount allocated in the SWCAP. In addition, a condition must be made in the negotiation letter that this cost is subject to final approval.

IX. DEPARTMENTAL ADMINISTRATION

Departmental Administration (DA) expenses are those that have been incurred for 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. The DA rate component usually consists of 4 broad categories:

1. College or School administration (the administrative expenses of the dean's office of each college or school)
2. Academic department administration (the administrative expenses of each academic department)
3. Residual academic department support costs (residual costs after application of the Direct Charge Equivalent or DCE formula adjustment)
4. Faculty Administrative Allowance or FAA (3.6 percent of modified total direct costs)

DA expenditures are not included as a line item expenditure on the institution's financial statements. The costs that make up the DA pool are reclassified from other functional categories during the development of the F&A cost rate proposal. Generally, DA costs are reclassified from the instruction and academic support functions shown on the financial statements.

Salaries and fringe benefits attributable to the administrative work of faculty, department heads and professional personnel conducting research and/or instruction should not be reclassified to the DA cost pool. This cost is covered by the 3.6 percent of modified total direct costs that is added to the DA component of the F&A cost rate. No documentation is required to support this allowance.

DA expenses include the salaries and operating expenses incurred in academic Deans' offices related to college or school administrative functions. Provided that the costs are treated consistently in like circumstances, DA may also include administrative and supporting expenses incurred within academic departments such as the salaries and wages

and fringe benefits of secretarial, clerical, administrative officers and administrative assistants, as well as the cost for travel, general operating supplies, and stock rooms, etc.

Costs associated with research, instruction, other institutional activities or any other non-administrative functions or activities should have been excluded during the screening of accounts process. This exclusion should be verified during the analysis of the DA pool.

The expenses in the DA pool should be allocated as follows:

1. The administrative expenses associated with each college or school Dean's office should be allocated to the academic departments within the specific college or school on a modified total cost (MTC) base.
2. The administrative expenses of each academic department, including that department's share of the Dean's office allocation, should be allocated to the appropriate department functions on a MTC base.

STEPS

COMMENTS

1. Obtain and examine detailed schedules supporting the allocation of Dean's DA to the appropriate academic departments.

Obtain detailed schedules supporting the allocation of DA by department. These schedules should show the total amount of DA for each department, the allocation bases for each department, and the DA allocated to each function by department and show the amounts of salaries, wages and fringe benefits for each of the following employee groups: (1) faculty, (2) professional researchers (e.g., research associates, research scientists), (3) other administrative personnel, and (4) technical.

STEPS

2. Review the expenses included in the Deans' offices, including a listing of the personnel assigned to the Deans' offices along with their job titles. If further support is needed, review the position descriptions and conduct follow up interviews.

3. Perform a comparative analysis to determine if the salaries of individuals accounted for in the Dean's office were included as academic department DA in the years prior to the 3.6 percent faculty allowance.

COMMENTS

It is not uncommon to find employees assigned to a Deans' office that are performing administrative activities that are not related to general college or school administrative duties. Student services administration is an example. These employees have job titles such as academic advisor, college advisor, director of student affairs, academic coordinator, and admissions analyst. Other employees may appear in the Dean's offices that have no college or school administrative responsibility. Examples might include a media specialist, development associates or a special events coordinator whose effort is related to public and community relations and fund raising. Professorial and faculty positions are frequently found in a Dean's office as well. Once again, these positions should be analyzed to determine what these people do. In most situations, faculty and professorial are assigned to a Dean's office because of seed funding or departmental funding in support of direct research or instruction activities. It is done more for convenience than because of their administrative responsibilities.

Such reclassifications could have the effect of circumventing the 3.6 percent faculty allowance. The university has the responsibility to substantiate all such reclassifications.

STEPS

4. Review the non salary expenses charged to the Deans' offices.

5. Obtain a listing of personnel by department whose salaries and fringe benefits are included in the professional administration DA pool. Review the job titles (classifications) and position descriptions of these employees. If necessary, interview selected employees to determine their major duties.

COMMENTS

The Deans' offices expenses may include costs that are not appropriate as DA. This situation frequently occurs at medical schools where medical liability (malpractice) insurance is recorded as a Dean's account expense. Such costs may only be claimed as a direct cost.

The administrative salaries and fringe benefits of professional business or administrative officers are not covered by the 3.6 percent allowance. These costs may be included in the DA pool as long as they have not been directly charged to Federal sponsored programs or have been adjusted through the direct charge equivalent (DCE) calculation. Some examples of these administrative positions are: business officers, department administrators, administrative assistants, and budget officers.

STEPS

COMMENTS

6. It is quite common for universities to charge sponsored projects directly for department administrative and clerical salaries and other administrative personnel. The remaining salaries for these administrative and clerical personnel are usually assigned to the DA cost pool before a similar charge or assignment of costs is made to instruction. This practice is referred to as inconsistent costing. The negotiator should request a list of title codes that identifies how each title code is treated in the DCE calculation. It should also show the total costs associated with each title code and the charges made to Federal sponsored accounts versus non-Federal sponsored accounts versus unrestricted institutional funds. This schedule or list will

The efforts of faculty and other professional personnel conducting research and/or associated with the development of contract proposals, and grant applications, (bid and proposal) regardless of their funding source are covered by the 3.6 percent allowance and should not be included in the DA pool.

Directors of research units and other comparable titles are not mentioned specifically in the Cost Principles with regards to the 3.6 percent allowance. However, because a director of a research unit has duties that are similar to a department head, his or her salary and fringe benefits would be covered by the 3.6 percent allowance.

Inconsistent costing exists when a university charges support costs directly to sponsored activities and then assigns similar support costs attributable to non-sponsored activities to the DA cost pool. If it is determined that a university has inconsistent costing practices in this area, corrective action is usually accomplished through a "Direct Charge Equivalent" (DCE) adjustment. See the following Section for guidelines on the use of DCEs. The DCE adjustment may similarly be applied to non-salary expenditures in the DA cost pool.

The salaries and wages of administrative and clerical staff should normally be treated as F&A costs. Direct charging of these costs may be appropriate where a major project or activity explicitly requires and budgets

STEPS

identify the appropriateness of title code classification for the DCE adjustment.

7. Determine whether the supplies and other non-labor expenses included in DA for any departments are unusually high. Review those departments' supplies and expense accounts to detect whether any of the accounts are strictly

COMMENTS

for administrative or clerical services and the individuals involved can be specifically identified with the project or activity.

In general, the Cost Principles state that the salaries of administrative and clerical staff should usually be treated as F&A costs, not direct costs. However, direct charging for these costs may be appropriate where the nature of the work performed under a particular project requires an extensive amount of administrative or clerical support which is significantly greater than the routine level of such services provided by academic departments. The costs would need to meet the general criteria for direct charging in Part 200.413 of the Cost Principles, i.e, "be specifically identified with the project or activity"; "relatively easily with a high degree of accuracy" and the special circumstances requiring direct charging of the services would need to be justified to the satisfaction of the awarding agency in the grant application or contract proposal.

Whether or not administrative and clerical staffs are considered appropriate to direct charge to Federal programs under the Cost Principles does not alleviate the need for the DCE adjustment.

The departmental supplies and expenses may include unusually large accounts which are strictly instructional in nature, such as lab or chemical supplies, glassware, or computer costs in some circumstances. These expenditures are usually direct costs and are frequently

STEPS

COMMENTS

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|---|---|
| instructional accounts. | large enough to cause distortions in the amount assigned to DA. |
| 8. Calculate a departmental DA rate for each department. | This step can help locate departments with unusually high DA rates and might, therefore, pinpoint departments with inequities in the DA cost category. |
| 9. Reconcile the total organized research, other sponsored activities, instruction and other institutional activities MTDC bases for all departments to the corresponding MTDC bases used in the F&A rate proposal step-down. | |
| 10. When dealing with a medical school, determine whether DA costs are allocated to the faculty medical practice plan (FMPP). If not, determine if the appropriate Dean's office or academic departments perform any administrative activities to support the FMPP. | The medical school dean or other officials may be responsible for the quality of patient care provided by the physicians in the faculty medical practice plan. They may also be involved in determining the amount of time each physician devotes to teaching and patient care; and in determining the amount that each physician will be paid from the practice plan. DA services may also be provided to the practice plan by other department administrative and support personnel. See Section XII.C. for a further discussion of faculty medical practice plan issues. |

STEPS

COMMENTS

11. When reviewing an F&A rate proposal for a medical school, determine if there are any service contracts between the medical school and any local hospitals or medical centers. If such contracts exist, determine what roles are played by the Deans, department chairperson or other administrative officials in the developing, negotiating and administering the contract.
12. If the medical school owns or operates a hospital, determine how the hospital is treated in the allocation of DA.

Depending on the results, some DA costs may need to be allocated to these contracts.

The medical school Dean as well as other staff of the Dean's office or academic departments may be involved in the administration of the hospital. If this is the case, then the hospital should receive an allocation of DA.

DIRECT CHARGE EQUIVALENT

Universities generally do not treat academic department support costs (e.g., the salaries of administrative and clerical staff, office supplies, postage, local telephone etc.) consistently. For example, administrative and clerical salaries are often charged directly to sponsored projects but not to instruction. The balances of administrative and clerical salaries that are not charged directly to sponsored projects are included in DA. This is a classic example of inconsistent costing and is not in compliance with the Cost Principles. This inconsistent costing practice raises a concern regarding the appropriate amount of the balance cited above that should be included in the DA pool, if any. The method developed by the government that gives recognition to this inconsistent costing is the Direct Charge Equivalent (DCE). The DCE is designed to compensate for this inconsistent costing. The DCE makes a correction for the inconsistency by calculating a reduction to the DA pool which represents the imputed value of departmental support costs related directly to non-sponsored activities.

An OMB memorandum dated, May 17, 1994, provided the following guidance: "Where direct charges for administrative and clerical salaries are made, care must be exercised to assure that costs incurred for the same purpose in like circumstances are consistently treated as direct costs for all activities. This should be accomplished through a Direct Charge Equivalent or other mechanism that assigns the costs directly to the appropriate activities."

STEPS

1. It would be very unusual if a university did not have to develop a DCE.

COMMENTS

The university's charging practices for administrative and clerical salaries and other non-salaried costs can be determined by reviewing various accounting and proposal documents. See section IX. Departmental Administration step 6 for more information.

STEPS

COMMENTS

	<p>Charging patterns can vary among the various academic departments within a university, therefore a DCE should be calculated department-by-department.</p> <p>The DA costs for each academic department should be reviewed to determine if there are support costs related to patient care activity, faculty medical practice plans, or potential recharge activities such as electronics shops, paint shops and fabrication shops. Support costs related to these activities are not considered DA and should be eliminated from the departmental support costs before computing the DCE ratio for each department.</p>
<p>2. Obtain information supporting the institution's computation of the DCE, including:</p> <p>a. MTDC and S&W figures for organized research, instruction and other institutional activities for each department.</p> <p>b. A summary of departmental support costs charged to sponsored projects for each department.</p>	<p>Almost all institutions use special data base software for the development of their F & A rate proposal. The calculation and application of the DCE is usually a standard module. Information should be readily available or easily generated from their data base.</p> <p>This summary should be by object or sub-account code for both salary and non salary costs charged directly to sponsored accounts. Obtain a schedule that shows both Federal versus non Federal sponsored account charges, unrestricted account charges and total costs</p>

STEPS

- c. A schedule of departmental support costs assigned to DA showing salary and wages and non-labor costs for each department.
 - d. A list of each job title (title code classification) included in the DCE calculation by department including the salary amounts in total by job title.
3. Review the charging pattern of administrative positions in major organized research departments. Compare the job titles (classification) of employees directly charged to sponsored activities to those employees included in the DA pool as 100% DA (see DA step 6).

COMMENTS

for the object or sub-account code.

The University should provide a list of all title codes and an associated letter designator explaining how each title code is treated in the DCE formula (100 percent as DA administration or part of the DCE).

In those cases where the salary for job titles (classification) are included 100 percent in the DA pool and were also directly charged to sponsored activities, the DCE ratio is understated and the DA pool is overstated. Where a significant amount (over five (5) percent) of salary for a specific job title is directly charged to sponsored accounts then the salary associated with the job title (classification) must be adjusted through the DCE before assigning the remaining costs (if any) to DA.

STEPS

4. The DA component must be recomputed after making the DCE adjustments.

COMMENTS

The DA component should be recomputed for each department.

In addition to reducing the DA pool for the DCE adjustment a pro-rata portion of the cross-allocations associated with the DCE adjustment should also be removed from the DA pool.

The revised departmental DA amounts should be added together to arrive at the DCE adjusted DA pool for the entire institution.

In addition to adjusting the DA pool, the instruction MTDC base should also be increased by the DCE amount, which will affect the allocation of G&A and DA. This should be done automatically when using an automated system.

Preferred DCE Methodology – Sponsored Projects DCE

1. The preferred DCE methodology is based on the following assumption: Within each academic department, the ratio of departmental support costs to the salaries and wages (S&W) for non-sponsored activities is the same as the ratio of departmental support costs to the S&W charged directly to sponsored activities.

$$\text{DCE Ratio} = \frac{\text{Support Costs Charged Directly to Sponsored Activities}}{\text{S\&W of Sponsored Activities (Net of support S\&W)}}$$

2. Assume the following information is known about a particular department in the University:

- Sponsored Research S&W (S&W_{SR}) = \$1,100,000
- Instruction & Departmental. Research S&W (S&W_{I&DR}) = \$2,000,000
- Departmental Support S&W in DA pool (DS_{S&W}) = \$500,000
- Departmental Support Non-Labor Costs in DA pool (DS_{N-L}) = \$250,000
- Departmental. Support S&W charged directly to SR (DS_{SR}) = \$100,000
- The University has not allocated any Departmental Support to I&DR.

3. The DCE is computed as follows:

$$\text{DCE Ratio} = \frac{DS_{SR}}{S\&W_{SR} - DS_{SR}} = \frac{\$100,000}{\$1,100,000 - \$100,000} = .10$$

The .10 DCE ratio is then applied to the $S\&W_{I\&DR}$ of \$2,000,000 to arrive at the DCE adjustment for S&W of \$200,000. Consequently, the $DS_{S\&W}$ of \$500,000 is reduced by \$200,000 to arrive at the allowable $DS_{S\&W}$ totaling \$300,000.

A separate DCE computation should be made for departmental non-labor costs. The DCE for non-labor costs should be computed in the same manner as the prior example for salaries and wages, except non-labor costs should be used in the calculations instead of support S&W. For the purposes of this illustration, it is assumed that the DCE adjustment for non-labor costs is \$100,000.

The total DCE adjustment then is \$300,000 (\$200,000 & \$100,000) and the departmental support costs which remain as DA are $(\$500,000 + \$250,000) - \$300,000 = \$450,000$. A pro-rata portion of cross-allocations should also be adjusted.

If this department had other direct activities (e.g., public service), then the DCE ratio developed would also be applied to the S&W of these direct activities.

The DCE adjustments should be made for each department for which the university is claiming DA.

It is possible that after computing a DCE adjustment the residual departmental support costs are a negative number. Under these circumstances, the departmental support costs available as DA would be zero. A negative number should not be used because costs cannot be disallowed that have not been incurred.

This particular DCE methodology can be applied on a campus-wide basis if the appropriate department data is not available. If a campus-wide DCE is calculated, the DCE ratio would be applied to the entire DA pool. This is not the preferred adjustment.

X. SPONSORED PROJECTS ADMINISTRATION

Sponsored Projects Administration (SPA) expenses are limited to those incurred by a separate organization(s) established primarily to administer sponsored projects, including such functions as grant and contract administration (Federal and non-Federal), special security, purchasing, personnel administration, and editing and publishing of research and other reports. They include the salaries and expenses of the head of such organization, assistants, and immediate staff, together with the salaries and expenses of personnel engaged in supporting activities maintained by the organization, such as stock rooms, stenographic pools and the like. Among others, SPA activities normally include proposal tracking, proposal review, (e.g., salary rates), award budget monitoring and final expenditure report preparation. This category also includes an allocable share of fringe benefit costs, depreciation, operations and maintenance expense, and G&A expense. Appropriate credits to SPA should be made for services provided to other functions or organizations. The expenses in the SPA category should be allocated to the major functions of the institution under which the sponsored projects are conducted on the basis of the modified total costs of sponsored projects (Federal and non-Federal). The extent of the CAS review of expenses in the SPA category should be determined by the materiality of the amount allocated to research. Sponsored projects administration expenses, combined with general administration and general expenses, departmental administration expenses, and student administration and services expenses, are limited to 26 % of modified total direct costs.

STEPS

COMMENTS

1. Assure that SPA includes only costs incurred by separate units established primarily to administer sponsored projects.
2. Obtain a list of the organizational units in the SPA cost category. Review the discrete units to determine their functions and activities.

If costs are reclassified into the SPA cost pool from other areas, the costs should be reviewed to determine if the transfer is appropriate.

Verify that the institution performed a screening of accounts. Request additional detail for SPA units with unusually large salary costs and/or non-salary costs. Single audits should not be charged to the SPA pool unless the institution treats other institutional audits in a consistent manner.

STEPS

3. Obtain a list of the employees and their job titles assigned to each SPA unit along with the percentage of each employee's effort charged to the unit.

COMMENTS

Each employee whose salary is included in SPA should be assigned 100 percent to a separate organization that exclusively or primarily benefits sponsored agreements. Work performed within SPA that does not benefit sponsored projects should be charged directly to the benefiting function. That work should not constitute a significant portion of an employee's total effort.

Effort associated with the preparation of contract proposals and grant applications (bid and proposal) are inappropriate charges to SPA. According to the Cost Principles, proposal costs should be allocated to all activities of the institution, and should preferably be included in G&A.

STEPS

4. If the SPA pool includes consulting fees for the development of special cost studies related directly to the conduct of Federal sponsored projects and the F&A rate proposal, effort should be made to insure the university charges similar consulting fees and studies directly to their benefiting activities.
5. Review the SPA pool for costs that were previously classified as DA or G&A.
6. Verify that the base used to distribute SPA costs includes the modified total direct costs of all sponsored projects, both Federal and non-Federal, where appropriate.

COMMENTS

These special studies and consulting fees should normally be assigned to the G&A cost pool. If the university is not consistent in the treatment of these types of costs, then a reclassification from the SPA pool to the G&A pool would be appropriate.

These reclassifications may have been made to circumvent the 3.6 percent faculty allowance or a DCE adjustment. As a general rule, to be an allowable SPA cost there must be a direct line-reporting to the SPA Director or other SPA manager.

In some instances, university funded research projects do not flow through the SPA. When this is the case, those projects do not have to be included in the SPA distribution base.

XI. STUDENT ADMINISTRATION AND SERVICES

Student administration and services (SAS) are expenses incurred for the administration of student affairs and for services to students, including but not limited to the Dean of Students, student admissions and registrar, counseling and placement, student advisory services, health services, catalogs, commencements and convocations. The expenses included in these categories and other student related services should generally be allocated entirely to the instruction function, and subsequently to any sponsored agreements in that function. An allocation of SAS to organized research should be accepted only where an institution can clearly show that a given service benefits organized research. The allowable services should be associated with students performing work on organized research projects and the services must be analogous to fringe benefits or services the institution provides to its employees. An example of this type of expense might be student health services. However, since some universities treat student health services as a fringe benefit expense when developing a student employee fringe benefit rate, care should be taken to assure the cost is not treated as both a direct cost and an F&A cost.

Student administration and services expenses combined with general administration and general expenses, departmental administration and sponsored projects administration are limited to 26 percent of modified total direct costs. The SAS category should include its allocable share of depreciation, interest costs, operation and maintenance expenses and fringe benefit costs. The negotiator should also ensure that space is properly identified and classified to the SAS function and that SAS expenses are not included in the other administrative pools.

XII. OTHER AREAS

A. FRINGE BENEFITS

Fringe benefits include all benefits paid by an organization to, or on behalf of, its employees. Examples include vacation, holiday, sick leave pay, and other paid absences; employee health, life, and disability insurance; post-retirement benefits (including pensions); social security taxes; unemployment compensation; worker's compensation, sabbatical leave, child care and tuition remission. Fringe benefits do not include tuition remission provided to an employee's family or to students. See Step 12. of this section and Section XII.E. for further discussion. Fringe benefits also do not include costs associated with the administration of fringe benefits unless those costs were included as fringe benefits prior to May 1, 1991, before the implementation of the 26% administrative cap, unless specifically approved by the cognizant agency for indirect costs.

The nature of the fringe benefit costs review will be governed by the organization's practices for budgeting and charging fringe benefit costs on Federal awards:

- If the organization uses a fringe benefit rate for both budgeting and charging purposes, the rate will be reviewed annually. During an institution's base year, the F&A rate and the fringe benefit rate will be reviewed and negotiated concurrently. The review should include an evaluation of the development of the rate as well as an evaluation of major and sensitive cost elements (i.e., the implementation of FASB Statement 106, Employers Accounting for Post-retirement Benefits Other Than Pensions). The negotiated rate should be included in the F&A cost negotiation agreement.
- If the organization budgets and charges fringe benefits based on specific identification of each benefit to individual employees, or uses estimated fringe benefit rates for budgeting purposes but uses specific identification system for determining their actual charges, the review should normally be limited to an evaluation of the organization's fringe benefit policies and its policies and procedures for determining and assigning the costs of the benefits to Federal awards. Primary emphasis should be given to major and sensitive cost elements.

- If the organization uses a "hybrid" system where certain benefit costs are charged based on a rate and other benefit costs are charged based on specific identification, the costs charged based on a rate will be subject to the review described in the first section above. The costs charged based on specific identification will be limited to the review in the second section above.
- Fringe benefit costs included in F&A costs will be reviewed as part of the normal review of F&A costs.

In order to avoid the necessity of making retroactive adjustments to the fringe benefit costs claimed on individual awards, the rates should be negotiated on a permanent (either predetermined or fixed) basis.

STEPS

COMMENTS

1. The following information should be requested:

- a. A listing of the fringe benefits paid by the organization
- b. A copy of the current fringe benefit policies
- c. The method used for budgeting and charging the cost of each benefit to Federal awards
- d. Whether the organization anticipates any changes to its fringe benefit policies or budgeting/charging method(s) in the future.

If the organization uses a fringe benefit rate for charging federal awards, the annual costs should be included in the listing. A break-out of the costs of paid absences should not be requested if they are included in gross salaries.

After the initial submission of these policies, only changes to the policies should be requested in subsequent years.

This information will be included in the Negotiation Agreement.

STEPS

COMMENTS

- e. A fringe benefit rate proposal

2. Review previous negotiation file to determine whether adjustments or problems were found. If so, determine whether the problems have been corrected.

3. Determine whether the organization treats the costs of the benefits consistently.

4. Determine whether the organization's fringe benefit policies are applied on a non-discriminatory basis as between employees working on Federally supported projects and employees engaged in other activities of the organization.

This is only required if the organization uses a fringe benefit rate for charging purposes. The proposal should be based on the organization's most recently completed fiscal year, and be reconciled and cross-referenced to the organization's audited financial statements.

It is not necessary that all benefits be treated in the same manner. However, the costs of each benefit must be treated consistently as a direct charge via a fringe benefit rate, as a direct charge through specific identification to individual employees, or as an indirect charge.

Verify that the costs included in the fringe benefit pool are not also included in the F & A rate pool. Examples of potential duplicate costs are Fringe Benefit Administration and Security Costs.

STEPS

5. Determine whether the benefits are reasonable.

6. Determine whether rebates and other applicable credits are properly considered in determining the costs (e.g., rebates of unemployment compensation insurance, health insurance rebates, life insurance dividends, etc.).

7. For pension plan costs, determine:
 - a. Whether the costs assigned to the fiscal year are determined in accordance with generally accepted accounting principles (GAAP).

COMMENTS

Examples of unreasonable fringe benefits include: mortgage subsidies, discounts on athletic/civic activities, bookstore discounts, etc.

Rebates and credits are often found in a breakdown of miscellaneous income from the audited financial statements.

For defined-benefit plans, emphasis should be given to ensuring that:

- a. The costs of the plan are assigned to each fiscal year based on an actuarial study.

- b. Past and prior service costs are amortized over a period of time not less than 10 years.

- c. The actuarial computations take into account unrealized as well as realized gains and losses on pension fund investments.

- d. The amount assigned to a given fiscal year is **funded** within six months after the close of that fiscal year. Increases to normal and past service pension costs caused by a delay in funding the

STEPS

COMMENTS

actuarial liability beyond 30 days after each quarter of the fiscal year to which such costs are assignable are unallowable.

For defined-contribution plans, determine that the contributions required under the plan are actually made (**funded**) and that the costs are reduced by dividends and other applicable credits.

Section 200.431(g)(6)(iv) of the Cost Principles applied only to State and Local governments prior to the issuance of the combined December 2013 Cost Principles. An IHE converting to a GAAP acceptable actuarial cost method for pension costs will only be able to recover their unfunded pension liability in a conversion to a GAAP acceptable actuarial pension cost method for the fiscal years starting on or after December 26, 2014. The unfunded pension liability for fiscal years beginning prior to December 26, 2014 for an IHE making a conversion is not allowable.

Also for the fiscal years starting on or after December 26, 2014, the amounts funded by the IHE in excess of the actuarially determined amount for a fiscal year may be used as the IHE's contribution in future periods where the IHE's funding is below the actuarially determined amount (up to that fiscal year's actuarially determined amount).

For state IHEs it may be disclosed that the IHE's

STEPS

COMMENTS

- actuarially determined pension contributions exceeded the Governmental Accounting Standards Board (GASB) Statement No. 68 calculated pension expense. However, 2 CFR 200.431(g)(3) only allows pension plan costs determined in accordance with GAAP (i.e., GASB 68). The Office of Management and Budget (OMB) is aware of this issue and is currently considering revising the regulations. Therefore, CAS may allow the actuarially determined pension contributions but reserve the right to revise this agreement to disallow the pension contributions in excess of the GASB 68 calculated pension expense, if OMB does not revise the regulation or issue an exception.
- b. Whether the plan complies with the Employee Retirement Income Security Act (ERISA).
- ERISA is a federal law that establishes certain standards which private pension plans must meet and imposes penalties (e. g., excise taxes) for non-compliance with the standards. Excise taxes on accumulated funding deficiencies and prohibited transactions of pension plan fiduciaries imposed under ERISA are unallowable.
- Premiums paid for pension plan termination insurance are allowable; however, late payment charges on such premiums are unallowable.
- c. Whether the organization credits the fringe benefit pool for unvested contributions made by
- Consider the university's treatment of the unvested contributions.

STEPS

the organization and included in the fringe benefit pool in prior years for employees no longer employed by the organization.

8. For postretirement benefits other than pensions, determine:
 - a. Whether the costs assigned to the fiscal year are determined in accordance with generally accepted accounting principles.

COMMENTS

FASB Statement 106, Employers' Accounting for Postretirement Benefits Other Than Pensions, issued in December 1990 and effective for fiscal years beginning after December 15, 1994 (for nonpublic enterprises), and as amended by FASB Statement 132 issued in February 1998, establishes accounting standards for employers' accounting for postretirement benefits other than pensions. Its primary focus is postretirement health care benefits. It changed the typical practice of accounting for postretirement benefits on a pay-as-you-go (cash) basis by requiring accrual (during the years that the employee renders the necessary service) of the expected cost of providing those benefits to an employee and/or the employee's beneficiaries and dependents.

Transition obligations for postretirement benefits are costs arising from the failure to accrue the accumulated postretirement benefit obligation in earlier periods. FASB Statement 106 measures transition obligations as the unfunded and unrecognized accumulated postretirement benefit obligation for all plan

STEPS

b. The amount funded.

COMMENTS

participants. The Statement provides two options for recognizing the transition obligation: 1) the transition obligation may be recognized immediately or 2) amortized over a period not to exceed twenty years with disclosure of the unrecognized amount. For budgeting and charging on Federal programs, the transition obligation will be allowable if funded and amortized over twenty years.

Postretirement benefit costs will be based on the lesser of amounts funded or amounts accrued. In addition, the following cost principles will be applied:

- Interest adjustments in current or future years, caused by delays in funding a reasonable estimate of the actuarial liability beyond thirty days after each quarter of the year to which such costs are assignable, are unallowable.
- Earning of investment income on reserves must be credited to those reserves. If reserves are not invested, imputed earnings will be credited to the reserves at the governmental unit's investment rate.

STEPS

9. If the organization charges all or some of the costs of paid absences (vacation, holiday, sick leave, etc.) on an accrual (when earned) basis, determine whether the amount accrued is properly determined.

COMMENTS

Most grantees and contractors charge the costs of paid absences on a cash basis as part of gross salaries and wages (i.e., when the employee is on leave, the project(s) he or she is working on continues to be charged for his or her salary). However, some organizations set up accruals for these costs and charge them separately from salaries. When accruals are used, they should normally apply only to paid absences which represent a definite liability of the organization (i.e., the organization must compensate the employee for the amount earned if the employee terminates his employment with the organization). However, if the organization can demonstrate that the accruals are properly adjusted by experience factors to reflect actual absences taken, the accruals may be accepted even where they do not represent a definite liability.

Terminal Leave is defined as earned vested leave that is unused at the time of an employee's termination of employment. The cost of this leave may be included in the fringe benefit cost pool if all terminal leave costs are treated consistently as fringe benefit costs. If not in the fringe benefit cost pool, it may not be equitable to charge the cost of this leave to an award or to the last grant charged. The development of an approved recharge rate for the development of a reserve or a separate terminal leave rate for the institution may be considered.

STEPS

COMMENTS

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| 10. When paid absences are included in the fringe benefit rate, determine whether they are excluded from the salary and wage base. | Verify that the negotiation agreement identifies the treatment of paid absences, and that the statement is consistent with the organization's treatment in the proposal. |
| 11. Review the organizations treatment of sabbatical leave. | If sabbatical leave is included in fringe benefits, determine that the aggregate charges to all work of the organization during the base period is reasonable in relation to the organization's actual experience under its sabbatical leave policy. The sabbatical leave policy must be uniform for persons engaged in instruction and persons engaged in research. |
| 12. Determine whether tuition remission for an employee's family members or for students working on research projects are included in the organization's fringe benefit rate or F&A cost rate. | For fiscal years beginning after September 30, 1998, tuition remission support for dependents of employees is not allowable as a fringe benefit or F&A expense. For tuition remission for students see Section XII.E. for further discussion. |
| 13. Ensure that any fines or penalties under the Affordable Care Act are excluded. | 45 CFR 75.477(b) makes any payments or assessments imposed on an employer as a result of the employer's failure to offer to its full-time employees (and their dependents) the opportunity to enroll in minimum essential coverage under an eligible employer-sponsored plan unallowable for Federal awards from an HHS awarding agency. |
| 14. Reconcile the fringe benefit rate calculation to the organization's financial statements. | |

STEPS

COMMENTS

15. Ensure that compensation for all employees receiving the fringe benefits is included in the fringe benefit rate calculation base.
16. Determine whether multiple rates for different classes of employees are needed.
17. Determine whether there are any benefit costs which should be assigned directly to a given employee(s) rather than to all activities through a rate (e.g., a special benefit provided only to one employee or a small group of employees).
18. Determine whether any changes are expected in the level of benefits or charging practices that would affect the rates in future years.

The compensation includes salaries and wages and payments in addition to basic compensation (e.g., amounts reported on IRS Form 1099, bonus payments, and awards). This may include compensation of employees working for affiliated or related organizations.

If the organization provides a substantially different level of fringe benefits to different classes of employees and the cost of those benefits in relation to the salaries of the employees differs significantly, a separate rate for each class must be considered.

STEPS

- 19 If an organization proposes a new fringe benefit cost in the pool, ensure that the cost of the new component is excluded from the calculation of the carry-forward.

20. If a fixed rate was established for a prior year, determine whether an appropriate adjustment (carry-forward) to compensate for the difference between the costs used to compute the rate and actual costs has been made.

COMMENTS

Since the new fringe benefit cost was not included in the calculation of the fixed rate for the year being finalized, it should not be included in the carry-forward calculation. By doing so would over-state the carry-forward.

If carry-forward amounts are calculated for multiple rates, verify that the carry-forward amounts are determined on a discrete basis.

B. SPECIALIZED SERVICE FACILITIES (SSF)

A specialized service facility is a service center that provides highly complex or specialized services that include, but are not limited to telecommunication centers, super computers, animal care facilities (vivariums), wind tunnels and reactors. The costs for these services should be charged directly to the users through a billing rate mechanism. Billing rates should be calculated for each SSF that do not discriminate between Federal and non-Federal users including internal university activities. The billing rates should be designed to recover the aggregate costs of providing the service and shall include both direct and an allocable portion of F&A costs. Billing rates must be adjusted biennially to adjust for under or over recoveries. Facility costs must be allocated to the SSF based on identifiable square feet associated with each SSF and the facility costs should be included in the appropriate billing rates. If an institution chooses not to include the facility costs in the billing rates, then the applicable facility costs must be assigned to other institutional activities (OIA). Facility costs associated with an SSF should not be allocated based on revenue generated. If administrative costs (GA, SPA or DA) are allocated to the SSF and included in the billing rate, the F&A MTDC base should exclude the recharge costs.

STEPS

COMMENTS

1. Review the university's policies for establishing SSFs from other recharge service centers.

A university may have several hundred service centers, but not all of them will be classified as an SSF. The university should have a written policy describing the guidelines used to identify an SSF from a recharge center. The negotiator should be aware that a university might treat service centers that are largely used by Federal projects as an SSF, while the costs of service centers primarily used by non-research functions are treated as either G&A, DA or O&M. The negotiator needs to look at the nature of the services being provided by the service center before making a decision on categorizing a recharge center as an SSF.

Request a listing of the service centers (recharge and

STEPS

2. Select several SSFs where charges to Federal programs are more than 50 percent of the total operational costs. Determine the following:
- When was the SSF established?
 - How was the SSF initially funded?
 - Does the SSF have financial statements?
 - How often is there a reconciliation of billed charges to actual costs?
 - Do the billing rates include only allowable costs (direct as well as F&A costs)?
 - Are all users (including outside users) billed at the same rate for the same services?
 - What is the unit of service that is used for developing the billing rates and determining the charges?
 - How are over and under recoveries handled?

COMMENTS

SSFs) along with the total costs of operations, the total costs billed and the total amounts billed to Federal projects for the year under review. Service centers can be identified through a review of cost transfers.

An SSF will usually have a formal published schedule of the billing rates. Users are charged based on the number of service units used, such as, hours or minutes of use, number of installations, animal days etc. Variances between the billed costs and actual costs should normally be treated as adjustments to future billing rates. For reconciliation purposes, revenue should include all revenue (including imputed revenue for unbilled services or services provided at a discount to certain users). The negotiator should also verify that SSF operating costs and losses are not included in the proposed F&A costs. Losses may be improperly included in the G&A or DA cost pool. Balances should be reviewed to make sure they are considered in developing future year rates. All transfers out of the fund, as well as surpluses and deficits should be reviewed. Fund deficits should not be transferred to F&A cost pools and surpluses should not be diverted for other uses. Surpluses and deficits associated with multiple service units within SSF must be treated individually within each unit. Surpluses and deficits may not be used to off-set other units of service.

STEPS

COMMENTS

3. Determine that F&A costs are properly allocated to all SSFs.

The allocation of F&A costs to a SSF is necessary to assure that these costs are assigned to the users of the services rather than to general overhead. However, it may not be necessary to require these allocations if the effect on the F&A cost rate is nominal (e.g., one tenth of a percentage point). It should be noted that the 26% limitation on the reimbursement of administrative costs is not applicable to specialized service center charges. Institutions should not add new specialized service facilities in order to exclude administrative costs which would be subject to the 26% limitation on administrative costs. Institutions should not change their accounting or cost allocation methods which were in effect on May 1, 1991.

SPECIAL CONSIDERATION FOR ANIMAL RESEARCH FACILITIES (ARF)

Research involving animals has become more sophisticated over the years and much of that research is now being performed within the confines of a specialized service facility referred to as an animal research facility. Rooms are actually being used in the conduct of research, rather than serving as an SSF. As a result, guidelines were published in May of 2000 in the Cost Analysis and Rate Setting Manual for Animal Research Facilities (CARS) which permitted certain ARF room types to be classified as research space versus SSF space. These rooms are procedure rooms, operating and recovery rooms, isolation rooms and quarantine rooms directly related to research protocols, as well as rooms that house animals involved in research that are not generally removed from the facility for conducting research. An example of this would relate to an animal that is removed from the facility for a specialized procedure such as Magnetic Resonance Imaging (MRI). The animal is removed only for the MRI, which is part of the research protocol and then immediately returned to the ARF. Space that continues to be classified as ARF space and included in the billing rates are administrative offices, autoclave areas, food and bedding storage areas, employee locker rooms and scrubbing areas, cage washing areas, receiving areas and rooms housing animals that are routinely removed from the ARF to either research laboratories or to research classified animal facility space for conducting research.

In addition, to avoid potential over-allocations of G&A costs to animal charges, if the billing rates include an allocation of G&A costs, the animal charges may be excluded from the MTDC allocation base used to develop the organized research rate.

This guidance has been incorporated in the revised Cost Analysis and Rate Setting Manual for Animal Research Facilities (CARS) - May 2000, which is available on the NIH web site:
https://grants.nih.gov/grants/policy/air/rate_setting_manual_2000.pdf

STEPS

COMMENTS

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| 1. Request a copy of the space survey instructions for the ARF. | The ARF Director should have this information, since it is an integral part of the rate setting process, as delineated in the CARS manual. |
| 2. Review the space classifications to determine compliance with the revised guidance. | Compare space designated as research space with the animal facility rate setting supporting work-papers to |

STEPS

COMMENTS

3. Review the space used for joint services.

confirm that there is no duplication. Space designated as research should be reviewed to confirm that it relates directly to a research protocol and that the animals are not generally removed from the facility.

In situations where space, i.e., animal rooms, are utilized for joint purposes of ARF service and research, request supporting data on how the space was identified to ARF service. The institution should identify space to either ARF or research based on the specific space within the joint area considering the days the activity took place within the space.

C. FACULTY MEDICAL PRACTICE PLANS

A Faculty Medical Practice Plan (FMPP) is the primary mechanism for organizing and managing faculty clinical practice activity at an IHE’s Medical and Dental schools. FMPPs establish operating rules, and the policies and procedures for participating in the FMPP, determining faculty compensation levels and clarifying the overall administrative management of the FMPP between the IHE and the organization that administers the Plan. The FMPP can become a major revenue source for the institution, can serve to attract highly respected and heavily research funded faculty members, increase the funds available for faculty compensation, and fund other activities within the institution.

In conjunction with the review of an IHE F&A cost rate proposal, a review of the FMPP is recommended to verify the proper treatment of costs in the proposal. FMPPs are set up and administered differently depending on the circumstances at each institution. For instance, some FMPPs are administered by the medical school through the Dean’s Office and others are administered by a separate 501-c3 non-profit organization.

This section was developed to assist in reviewing the treatment of FMPPs and the primary objective is to assure that FMPPs are allocated their appropriate share of F&A costs.

STEPS

COMMENTS

1. Determine if the institution has a faculty medical practice plan.

Most medical and dental schools have some type of FMPP. These plans allow faculty to be involved in patient care activities. FMPPs normally function in a clinical department, such as Medicine, Obstetrics and Pediatrics. The negotiator should ask the institutional representative responsible for preparing the proposal if the institution has an FMPP and how it was treated in the F&A rate proposal.

STEPS

2. Request copies of all formalized agreements between the institution and the administrator of the FMPP. These agreements should include:
 - a. An organizational description of the FMPP;
 - b. Operating policies and procedures;
 - c. Responsibilities and authority for each institution;
 - d. Operating leases for space and/or equipment;
 - e. Non-capital items or services to be provided between the institutions.
3. Request copies of FMPP financial statements and expense details for the fiscal year under review.
4. Determine whether effort by faculty and support staff associated with the FMPP is addressed in the institution's activity reporting system.
5. Determine how the FMPP is treated in the F&A cost proposal.

COMMENTS

Many institutions have formal written agreements with the FMPP members or with the organization administering the FMPP. Organizational structure may vary. One institution may negotiate a different agreement with each academic department; another may have one institutional wide agreement. If formal written agreements do not exist, it is recommended that the negotiator meet with the FMPP administrator to discuss all administrative and operating aspects of the FMPP.

Many FMPPs generate a significant amount of revenue, requiring certified financial statements. Financial statements should be available from the FMPP administrator.

Some FMPPs are fully integrated into the institution's functional activities.

The degree of autonomy between the FMPP and the university; and the amount of supporting services (e.g., space related expenses, administrative and general services) the institution provides to the FMPP varies. Accordingly, a clear understanding of how and what services the institution considers allocable to FMPP

STEPS

COMMENTS

6. Review all FMPP plan agreement(s) and note the following:

a. Treatment of compensation paid to participants.

- Methodology utilized to pay bonuses above base payments.

- Compliance with NIH Salary Cap.

activity should be documented.

Most plans fund a portion of the participants' basic compensation package but are not always part of the activity reporting system. On August 4, 2005, the National Institutes of Health (NIH) released Notice Number NOT-OD-05-061 that provides the "Guidelines for Inclusion of Clinical Practice Compensation in Institutional Base Salary Charged to NIH Grants and Contracts". This notice provides revised criteria related to the inclusion of FMPP compensation in the institutional base salary. If the FMPP compensation is included in the institutional base salary then the FMPP activity must be included and accounted for in the institution's effort reporting and/or payroll distribution system.

Amounts paid above the basic compensation are normally considered bonus payments. Treatment of bonus payments for F&A cost and fringe benefit allocation should be reviewed. Excluding bonus payments from the allocation base should be evaluated to determine whether they are appropriate.

The NIH salary cap could have a significant impact on the institution, since combined reimbursements (institution/base FMPP payments) could easily exceed the annualized level of the NIH ceiling. In these instances any increment in excess of the limitation

STEPS

COMMENTS

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| | <p>must be included in the appropriate F&A cost MTDC base (bonus payments should be evaluated on a case-by-case basis). Fringe benefit base treatment should also be reviewed to determine if the FMPP payments should be included in the fringe benefits base.</p> |
| <p>b. Treatment of compensation paid to FMPP administrators and support staff.</p> | <p>This compensation is directly charged to the plan at most institutions. Compensation rates should normally be similar to other institutional employees performing similar functions. Determine if any portion of the support staff compensation is allocated to the university cost pools. If so, examine the allocation methodology. It should be noted that FMPP administrative support employees may occupy space in departmental administrative offices.</p> |
| <p>c. Treatment of fringe benefits.</p> | <p>The treatment of fringe benefits should be similar to other activities of the institution. When fringe benefits applicable to FMPP compensation are included in the university's fringe benefit pool, then the FMPP compensation must be included in the fringe benefit salary and wage base.</p> |
| <p>d. Treatment of support services (e.g., space related cost, Wi-Fi, telephone, medical records, postage, purchasing, personnel, etc.)</p> | <p>Compare to treatment noted in the proposal and determine differences (e.g., telephone and postage may be charged directly to the plan).</p> |

STEPS

COMMENTS

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| e. Treatment of malpractice insurance. | Treatment of malpractice insurance applicable to FMPP activities varies. Normally a portion of the "risk management" office would be allocable to this activity. Current regulations require that malpractice insurance shall be treated as a direct cost. (See Section XII.D. for further discussion of malpractice insurance.) |
| f. Treatment of costs related to billing and collecting patient accounts. | This function should be charged directly to the FMPP. |
| 7. Request summary analysis of plan expenditures by major expense classification and: | At some institutions, plans are established on a departmental basis and are not administered on an institution wide basis. If this is the case, select one or two departments with a significant amount of private practice activity for further review. |
| a. Reconcile to the institution's financial statements and/or FMPP financial statements (if available) and review all significant differences. | |
| b. Selectively review effort reports of faculty and support staff. | Review should include verification that effort reporting is in compliance with the institution's activity reporting system and the Cost Principles requirements, and is consistent with the NIH "Guidelines for Inclusion of Clinical Practice Compensation in Institutional Base Salary Charged to NIH Grants and Contracts". |
| 8. Determine the reasonableness of how FMPP costs are treated in the F&A cost proposal: | |

STEPS

COMMENTS

a. Equipment depreciation

- Determine how equipment depreciation is identified.
- Determine that jointly used equipment is properly allocated to the FMPP.

At most institutions, equipment related to the FMPP is specifically identified and charged to the FMPP.

Many departments have common equipment rooms, which may include jointly used equipment utilized by the FMPP. Selectively review usage logs and/or discuss with the Department Administrator.

b. How has space been identified to the FMPP?

- Was FMPP space included in the space use survey?
- Was FMPP space costs treated as an offset to the space related cost pools?
- Was all FMPP space identified?

At some institutions, the FMPP facility is housed in department space. At others, the FMPP is housed off campus or at an affiliated hospital. Space allocation to the FMPP may vary on a department by department basis. For example, in some departments faculty may see patients in their offices.

Treatment should be similar to other major functions of the institution.

Compare the offset to the amount that would have been allocated to the FMPP had it been handled as a major function in the space survey. The offset should at least equal the full allocable amount of depreciation, interest and O&M costs. Evaluate any differences.

At many institutions, FMPP space is not properly identified. During the space survey, the negotiator should note space related to waiting rooms, patient file rooms, examining tables contained within faculty offices, etc. FMPP brochures and online telephone

STEPS

COMMENTS

directories can be of assistance in identifying misclassified FMPP space. In addition, FMPP employees often occupy departmental administrative space possibly requiring an adjustment to the DA space.

c. General Administrative and General expenses.

- Are G&A costs fully allocated to the FMPP, similar to other major institutional functions?
- Determine how the costs for billing and collection of patient accounts are treated.
- Scan major expense items included in the G&A cost pool such as legal, accounting, consultants, insurance, etc.

The amount of G&A allocated to FMPP can vary depending upon organizational setup and operating procedures. For example, FMPP employees may not be hired by the institution; also the institution may not prepare the FMPP payroll. In many instances, the FMPP does not benefit from all G&A functions which might require the formulation of sub-pools. The negotiator should assure that the appropriate amount of G&A is allocated to the FMPP.

This activity is similar to a sponsored projects administration unit and should be charged directly to the FMPP. At some institutions, this activity is performed by a service bureau under contract to the FMPP.

Review G&A cost categories to identify any specific costs that could be related specifically to the FMPP. These items should be removed from the G&A expense pool.

d. Departmental Administration (DA)

STEPS

- Selectively interview Department Administrator(s) to determine their relationship with the FMPP.
- Review the treatment of FMPP activities in the allocation of DA.

COMMENTS

The degree of autonomy and the extent of departmental administrative support vary. At some institutions the plan reimburses the department directly for administrative support. An FMPP administrator, paid by the plan, may be physically located in DA offices requiring an adjustment for support services and cross allocations including depreciation, interest and O&M.

At most institutions a portion of FMPP revenues are used to fund DA personnel and activities. A selective review of these functions is necessary to verify that they are DA and not specifically related to the FMPP. In addition, at some institutions the FMPP funds positions directly which are excluded by the institution without considering support costs (supplies and services, etc.), and cross allocations.

D. MEDICAL MALPRACTICE INSURANCE

Malpractice insurance is the professional liability insurance subscribed to by a medical practitioner to insure against a loss resulting from a judgment against the practitioner. Current regulations require that medical liability (malpractice) insurance is an allowable cost of research programs only to the extent that the research involves human subjects or training of participants in research techniques. Medical liability insurance costs shall be treated as a **direct cost** and shall be assigned to individual projects based on the manner in which the insurer allocates the risk to the population covered by the insurance.

E. TUITION REMISSION EXPENSE

IHEs frequently employ graduate students on sponsored projects and waive some or all of their tuition as compensation for their effort. Since the waivers (referred to as tuition remission) are considered part of the students' compensation for effort performed on the projects, they are allowable costs under the Cost Principles. The Cost Principles require that tuition remission be treated as a **direct project cost**, unless the student is working in an F&A function. Tuition remission costs should not be included in a composite fringe benefit rate.

STEPS

1. Determine whether tuition remission costs are treated as direct or F&A costs and make adjustments as appropriate.

COMMENTS

The Cost Principles require that charges for tuition remission be treated as direct or F&A costs in accordance with the actual activity being performed. If a student works directly on a sponsored research project the tuition remission cost should be directly charged to that project. The only tuition remission that would be allowed as an F&A cost would be those related to graduate students who work in an F&A function, such as accounting or other administrative function.

Tuition remission for students working on sponsored projects or other activities should be consistently treated as direct charges to those projects or activities, not as F&A costs or part of a general fringe benefit rate. It is acceptable to treat the tuition remission as a special "tuition remission" rate for graduate students, or as part of a **special** fringe benefit rate for graduate students.

STEPS

2. If tuition remission costs are included in a general fringe benefit rate, make the appropriate adjustment to the fringe benefit rate.
3. Although tuition remission may be treated as a direct cost, tuition remission is excluded from the modified total direct cost base. The negotiator should determine whether the space occupied by those individuals compensated by tuition remission has been excluded.

COMMENTS

When tuition remission is excluded from the direct cost base, the negotiator should examine the space occupied by the individuals receiving the tuition remission. The space occupied by the individuals who are compensated by the tuition remission being excluded from the direct cost base, in lieu of salary and wage compensation, should be identified. This space should be classified as IDR or OIA. If an institution classifies the space occupied by these individuals as organized research, then the negotiator should either make an adjustment to the space classification or impute the salaries and wages plus applicable fringe benefits for these individuals and this calculation must be added to the organized research direct cost base.

F. **CONTRIBUTED EFFORT (COST SHARING)**

Cost sharing is that portion of a sponsored project not funded by the Federal government or a non-Federal sponsor. Cost sharing is important to identify and quantify because the costs should be included in the base for developing the F&A rate. The purpose of cost accounting standard CAS 9905.501 - Consistency in Estimating, Accumulating and Reporting Costs is to assure that educational institutions are consistent in how they estimate, accumulate and report costs. Costs should follow the project or activity, not the funding source. For example, a principle investigator who commits 50% of their salary as effort to a sponsored federal research project (#600582) while only requesting 25% salary reimbursement has committed to cost sharing. The cost shared amount (25%), even if funded through an unrestricted institutional account, must be included as a cost of the sponsored research project #600582 and included in the base for developing the F&A rate. The cost allocation process related to cost sharing is not affected by funding decisions made by Federal or non-Federal awarding agencies.

The three forms of cost sharing are described below:

Mandatory cost sharing – mandatory cost sharing (which is not widely used anymore) is required by the sponsor as a condition of obtaining an award. When an award is received which requires mandatory cost sharing, the cost sharing becomes an institutional commitment, which the institution must provide. All mandatory cost sharing must be documented and included in the base for the F&A rate proposal.

Voluntary committed cost sharing - voluntary committed cost sharing represents a commitment made to a sponsored project either through the budget or through the narrative description. If an award is made to an institution that contains voluntary committed cost sharing, the institution is responsible for documenting that cost shared commitment and including it in the base for the F&A rate proposal.

Voluntary uncommitted cost sharing - voluntary uncommitted cost sharing (VUCS) is restricted to **only** university faculty (including senior researchers) effort that is over and above that which is committed and budgeted for in a particular project. Voluntary uncommitted cost sharing excludes effort devoted to a project that was originally committed by the faculty, including senior researchers, or is a result of a shift in workload. Voluntary uncommitted cost sharing does not need to be included in the organized research base or be reflected in any allocation of F&A costs.

STEPS

1. Request a copy of the institution's cost sharing policies and procedures.
2. Review cost sharing policies and procedures.
3. Request a copy of and review activity reporting instructions and system.
4. If the cost sharing included in the proposal appears low, it may be appropriate to perform a review of selected high dollar research departments. .
5. Request copies of grant applications, award documents, budgets, and supporting data for a sample of principal investigators and staff in the departments selected for review.
6. Request activity reports for those selected principal investigators and staff from the departments selected for review that are included on project awards.
7. Determine potential cost sharing adjustment(s).

COMMENTS

The DS-2, Disclosure Statement, should include or reference an institution's cost sharing policies and procedures.

Determine how an institution accounts for and documents mandatory and voluntary committed cost sharing.

Review instructions to determine if the issue of voluntary uncommitted cost sharing is addressed and accurately defined.

The departments selected should have a significant amount of Federally funded sponsored research.

Note that for most NIH awards, there is no formalized budget since most awards are made using the modular grant concept. Modular grant applications contain percentages of effort of personnel. Non-Federal awards may also have cost sharing requirements.

Compare the percentages of organized research effort reported on the activity report to the selected grant award document. Note any variances.

Many institutions have developed cost sharing systems that properly capture mandatory and voluntary

STEPS

COMMENTS

8. Develop a negotiation position for mandatory and voluntary committed cost sharing, if appropriate based on the review.

9. Determine that voluntary uncommitted cost sharing is being treated in accordance with the OMB memorandum.
 - Request a listing of significant workload shifts.

committed cost sharing through the use of shadow, tandem or companion accounts. These accounts are set up when the initial award is received to capture mandatory or voluntary committed cost sharing. These systems may be selectively tested by comparing the amounts reported to the grant award data (budget applications).

If a determination is made that mandatory and voluntary committed cost sharing is not properly identified, an adjustment is required. This should be based upon the results from the sampled departments, extrapolated to the entire organized research base. The applicable fringe benefits must be added to the cost shared salary amount.

OMB issued a memorandum clarifying the treatment of this cost. As noted in the memorandum, the grantee should have procedures in place preventing the shifting of voluntary committed cost sharing to voluntary uncommitted cost sharing.

University faculties including senior researchers are required to maintain their base workload schedule as noted in their appointment letter or activity schedule. This information is normally controlled by the faculty member's Dean or Department Chair. If significant workload shifts are taking place to accommodate additional effort on sponsored research projects then this shift must be reflected in the organized research

STEPS

COMMENTS

base. If the faculty member/senior researcher is not meeting their basic workload schedule then the effort related to research activities may be understated and should be adjusted.

G. INTERGOVERNMENTAL PERSONNEL ACT (IPA) MOBILITY PROGRAM RATES

The goal of the Intergovernmental Personnel Act (IPA) mobility program is to facilitate the temporary assignment of employees when the assignment serves a sound public purpose. IPA assignments are intended to facilitate cooperation between the Federal Government and non-Federal entities through the temporary assignment of skilled Federal employees to serve with eligible non-Federal organizations for a limited period without the loss of employee rights and benefits. Employees of state and local governments, Indian tribal governments, institutions of higher education and other eligible organizations may also serve in Federal agencies for similar periods.

The Department of Defense Procurement and Acquisition Policy (DPAP) has issued memorandum guidance (DPAP Memorandum dated October 17, 2003) which states that DoD agency personnel may provide for the reimbursement of indirect costs associated with an IPA program, provided that such costs are allowable and allocable and have been approved by the non-Federal entity's cognizant Federal agency. It should be noted that this DPAP Memorandum guidance is specific to IPA programs with the DoD. Reimbursement of indirect costs by non-DoD agencies will be determined by the agency that enters into the agreement.

The unique nature and arrangement of IPA agreements requires that care be taken to limit the allocated indirect costs to only the indirect costs whose functions benefit the IPA agreements. Generally speaking, these functional costs are included as part of the general administration (GA) and sponsored projects administration (SPA) cost pools. The IPA indirect cost pool should include only applicable benefiting administrative costs; and the IPA rate should apply only to the positions covered under the IPA mobility program.

The IPA cost pool is developed using the applicable IHE allocated costs from the (GA) and (SPA) cost pools in the current or last submitted F&A cost rate proposal. Only functions or categories that provide benefit to the IPA agreements should be included in the cost pool. Some functions or categories that may be considered include the applicable portions of:

- a) Contract and Grant Administration
- b) Finance Administration
- c) Employee/Labor Relations
- d) Human Resources
- e) Controller/Comptroller

These aforementioned functions or categories may include cross allocations. After the IPA cost pools are developed, the allocation percentages that are used in the F&A cost rate proposal for the appropriate MTDC function are applied to the cost pools. In F&A cost rate proposals that are prepared when IPA rates are already in effect, a separate MTDC function for IPA agreements should be developed. The MTDC base should include all IPA agreements, regardless of whether indirect cost is recovered or not. However, if an IPA rate is being developed based on the last submitted F&A cost rate proposal, then the appropriate MTDC function is the function that includes the positions covered under the IPA mobility program in the F&A cost rate proposal. Generally this is the organized research MTDC base or the instruction and departmental research MTDC base.

The calculated IPA cost pool is then divided by the total MTDC base in the F&A cost rate proposal that includes the IPA positions. The resulting IPA rate is generally lower than the institution's off-campus F&A rate and shall be published only if requested by the institution. The reimbursement of such costs is subject to granting agency approval by the agency entering into the IPA agreement.

H. AFFILIATED HOSPITAL SPACE INCLUDING VETERAN ADMINISTRATION FACILITIES

IHEs, particularly those with Medical Schools, often have affiliation agreements with hospitals. These affiliation agreements address a number of issues including, but not limited to, an IHE occupying space in the affiliated hospital, or a hospital providing administrative services to the IHE. In conjunction with the CAS evaluation of the IHE F&A rate proposal, a review of these affiliation agreements is also recommended to ascertain that each organization is properly accounting for and claiming costs. The objective is to assure that the costs associated with affiliation agreements are not being reimbursed twice; once through the IHE's F&A rate and again through the hospital's Medicare cost report.

NIH grants awarded to academic institutions where the research is being conducted at Veteran Administration (VA) facilities are treated differently than an affiliated hospital. The National Institutes of Health (NIH) prohibits NIH grants from reimbursing indirect costs associated with space occupied at VA facilities. This prohibition is addressed in the NIH Office of Extramural Research Policy Notice dated August 13, 2003 that is part of the NIH Guide for Grants and Contracts. The rationale behind the prohibition is that HHS policy prohibits payment of F&A costs to Federal Institutions. NIH asserts that the VA facility costs are supported through its' own Federal appropriations. Generally, the off-campus rate, if determined to be appropriate, should be applied to all NIH awards performed in VA space. However, in those situations where the IHE uses its' own equipment in the VA space, an additional factor may be added to the off-campus rate for equipment depreciation. In addition, if an IHE renovates VA space that is to be occupied by the IHE, then a deprecation factor for this cost is allowable to be added to the off-campus rate. However, no facility costs that were covered in the VA appropriation should be included in the F&A rate applicable to research conducted at the VA facility.

STEPS

1. Determine if the IHE has any affiliation agreements with a hospital.

COMMENTS

IHE and hospital affiliations are often disclosed in the audited financial statements. Formal written affiliation agreements between the IHE and the hospital should be available for review.

STEPS

2. Request copies of any formalized written affiliation agreements between the IHE and the hospital.

These agreements could include:

- a) Descriptions of leases or agreements for use of space and/or equipment.
- b) Descriptions of non-capital items or administrative services one organization will provide to the other.
- c) Descriptions of how the supporting service costs or space related costs will be billed to the IHE based on actual costs or allocated through the MCR.

3. Obtain the hospital's Medicare Cost Report (MCR) or equivalent form.

4. Determine the treatment of costs associated with the affiliated hospital. Are the space related and administrative service costs being claimed by the

COMMENTS

Many institutions have formal agreements with affiliated hospitals outlining the type and scope of work being performed, the space to be occupied and the administrative services that will be provided. It is also important to determine if the hospital bills the IHE for the costs of the services and the space or if the costs are determined through the normal MCR step-down process. If formal agreements do not exist, it is recommended that the negotiator meet with a representative group of hospital and IHE administrators to discuss all aspects of the affiliation.

The MCR is an annual report required of all institutions participating in the Medicare program. The MCR records an institution's total costs and charges. It also provides a step down of the hospital general service costs to both reimbursable and non-reimbursable hospital cost centers. The hospital's MCR often has a separate research line (usually Line 97.0) that identifies research costs and statistics.

The degree and amount of administrative support services and space related expenses the hospital provides to the IHE varies. Accordingly, it is important

STEPS

COMMENTS

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|---|--|
| IHE or by the hospital? | to understand what administrative services and space related costs are provided and how the costs are determined. It is also important to understand where the costs are recorded and claimed |
| 5. If hospital administrative support costs and space related costs are being claimed in the IHE F&A rate proposal, determine how the costs are treated in the MCR. | If a hospital directly bills the IHE based on actual costs for providing the space related and administrative support services, then an adjustment (credit) must be made to the applicable hospital cost pools. This is usually made on Worksheet A-8 (it should appear as a cost or revenue off-set). If the hospital allocates the costs to the IHE through the normal MCR step-down process in the non-reimbursable section, then an adjustment (credit) is not required. |
| 6. If hospital space is included in the IHE F&A rate proposal, verify that the corresponding space statistics are offset in the hospital's MCR (Worksheet B-1). | Space (ASF) is the allocation statistic for several MCR General Service costs (e.g. building, maintenance, operation of plant, housekeeping, etc.) If the space is claimed in the IHE's F&A proposal, then the space should be offset in the MCR (Worksheet B-1). |
| 7. Determine if patient care costs are included in the F&A rate proposal MTDC base. | The Cost Principles state that costs associated with patient care shall be excluded from the MTDC base. |
| 8. Determine if the cost pools in the F&A rate proposal combine expenses of both the IHE and hospital. | The negotiator should be aware that an IHE and hospital might combine a cost grouping, such as O&M, and then allocate the costs across combined ASF. If this is inequitable, a separate rate or subpool may be necessary, since the hospital's O&M cost per ASF may be higher than the IHE's. |

STEPS

9. The institution should confirm as to whether or not NIH research awards are conducted at a VA facility. If the institution conducts NIH research at a VA facility, the institution should explain how the VA space costs and the NIH grant costs are treated in the F&A rate proposal. A separate rate for NIH grants performed in a VA facility may need to be developed if the IHE off-campus rate is not appropriate.

COMMENTS

Costs for the use of VA facility space should not be included as O&M costs in developing the on-campus organized research F&A rate. Similarly, the direct costs for the NIH research conducted in VA facility space should not be included in the on-campus organized research MTDC base.

Verify that both the O&M costs and the direct research costs related to NIH research at the VA facility are not included in either the cost pool or the MTDC in the on-campus organized research F&A rate proposal.

Where it is determined to be appropriate, the IHE off-campus rate may be used for NIH grants performed in a VA facility; however this rate must not include space related costs from any other off-campus facilities.

I. F&A RATE EXTENSIONS

The Cost Principles 2 CFR part 200.414 (g) states that any non-Federal entity that has a federally negotiated indirect cost rate may apply for a one-time extension of their current negotiated indirect cost rates for a period of up to four years. This extension will be subject to the review and approval of the cognizant agency for indirect costs. If an extension is granted the non-Federal entity may not request a rate review until the extension period ends. At the end of the 4-year (or less than 4-year) extension, the non-Federal entity must re-apply to negotiate a rate.

The intent of allowing for F&A cost rate extensions is to minimize the administrative burden for the non-Federal entity. As such, documentation requirements to support an F&A cost rate extension should be kept to a minimum. The following information is required for an extension of the current F&A cost rates for IHEs that had their last F&A rate negotiated based on a long-form proposal:

- a) Copy of the last audited financial statement and last Single Audit report.
- b) A schedule showing the approximate research base for each year, beginning with the last reviewed base year up to the last completed fiscal year, plus a projection of the estimated research base for the next 4 fiscal years (or less than 4 years if the rate extension request is less than 4 years).
- c) Details of any significant changes to the **research space** since the last reviewed base year (new buildings, buildings closed, major renovations), plus a projection of any expected significant changes to the actual **research space** for the next 4 fiscal years (or less than 4 years if the rate extension request is less than 4 years).

STEPS

1. Confirm that the required information listed above has been provided with the request for an F&A rate extension.

COMMENTS

A recalculation of the F&A rates or a reconstruction of the rate proposal is not required nor should be required by the negotiator. The extent of the information in b) and c) above is a summary of the research base dollars and research square footage for the stated years, along with any applicable explanations.

STEPS

2. Determine the type of rates (final, provisional, predetermined or fixed) negotiated based on the last submitted F&A rate proposal.

COMMENTS

Current federally negotiated rates include only predetermined and final rates (not provisional or fixed rates). The IHE must have a current federally negotiated F&A cost rate to apply for an extension of F&A cost rates. A predetermined rate should not be expired at the time of the request for a rate extension. If final rates were the last permanent rates negotiated, and these rates are based on the latest applicable audit and completed fiscal year under 2 CFR 200 (beginning on or after December 26, 2014), those rates are considered current for this purpose and may be used to apply for an extension. For example, if an IHE's last fiscal year ended June 30, 2016 and rates are finalized based on the audit received before the end of March 2017 with the costs incurred through June 30, 2016, the organization could apply for a one-time extension before submitting the final rate proposal for fiscal year ending June 30, 2017. In this example, the IHE can request an extension covering fiscal year(s) 2017 through 2020.

IHEs with fixed rates (includes a carry-forward) cannot be extended. If an IHE with a fixed rate would like to take advantage of the flexibilities of the rate extension provision of the Uniform Guidance, the IHE would need to first negotiate a final or predetermined rate, which could then be extended, subject to the approval of the cognizant agency. The carry-forward for the last fixed year would have to be resolved in accordance with cognizant agency for indirect cost procedures.

STEPS

COMMENTS

3. Confirm that the request for a rate extension was submitted timely.
4. Confirm that the last negotiated rate with the IHE was based on an F&A rate proposal submission.

Requests for F&A rate extensions should preferably be submitted 60 days prior to the due date of the next F&A rate proposal. However CAS can accept extension requests submitted later than that. It is mandatory that the request be submitted prior to the expiration of a predetermined F&A rate(s).

Rate extension requests are not allowed if the last rate was based on a rate extension. This includes rate extensions for less than 4 years. In this case a rate proposal must be submitted for review by CAS. However subsequent one-time extensions (up to four years) are allowed if a renegotiation is completed between each extension request. Once there is a new negotiated F&A cost rate in effect, an IHE could request a one-time extension on that rate. For example, an IHE with a current negotiated rate for 7/1/16-6/30/17 requests an extension of that rate for 3 years, until 6/30/20. If approved by CAS, the IHE is required to submit a proposal and request a negotiation of a rate for the period beginning 7/1/20. Assuming this negotiation results in predetermined rates effective until 6/30/24, the IHE could then request an extension of the current negotiated rate at the end of this approved period (6/30/24), prior to the due date for the submission of the next proposal.

STEPS

5. Review the submitted information provided with the F&A rate extension request.

COMMENTS

The negotiator should examine the trend in the research base. If since the last submitted rate proposal there was a very large spike in the research base, or if the research base has been growing each year at a much greater pace than expected (for example a 10% or more increase per year), then the negotiator may not feel it is in the Federal government's interest to extend the current F&A rates. This large increase in the research base may result in significantly lower F&A rates. If this is the case, the negotiator can consider a short-term rate extension (1 or 2 years) or deny the rate extension and require the IHE to submit a proposal. If the research base has stayed relatively flat, increased modestly, or increased in line with inflation, then the rate extension may be considered.

The negotiator should also examine the research square footage trends. Caution should be taken in granting a rate extension where research square footage has decreased significantly. Perhaps a new building included in the last F&A rate projection, from which the current rates were negotiated, has significantly decreased its research square footage due to the inability to bring in new researchers. Again the negotiator may consider denying the rate extension or only allowing it on a short-term basis.

6. Review the prior work-papers and the prior negotiation notes.

The last rate negotiation and the results of that review must be considered in granting a rate extension. If there were significant pending issues affecting the

STEPS

COMMENTS

future F&A rates in the last rate proposal review which were expected to be corrected in the next proposal submission, then a rate extension would not be appropriate.

In addition, if the rate in the last year of a multi-year negotiation is not representative of the actual negotiated rates based on the review of the rate proposal, then extending that rate may not be appropriate. For example, in the last rate negotiation based on the submitted F&A proposal, a 3-year predetermined rate was negotiated and the negotiator determined that the negotiated rate was 49.0%. Since the first year of the 3-year period already began, in order to minimize the administrative burden on awarding agencies the negotiator and IHE agreed to a lower rate in the first year. The rates for the 3-year period are published at 46.0%, 49.0% and 52.0%, respectively. In this scenario, extending the rate of 52.0% would be inappropriate.

However if the last year's rate in a multi-year negotiation is higher due to a rate projection, then the negotiator should examine the data submitted with the extension request to determine if the prior rate projection was accurate based on the trends in the research base and square footage. If the negotiator is satisfied that the data is closely consistent with the data in the prior rate projection, then the rate extension may be considered.

J. FACILITY COST PROJECTIONS

Institutions are permitted to submit a facility cost projection proposal (FCPP) that supports the institution's claim that there will be significant increases to their facility costs due to new construction and major remodeling projects. The FCPP should be submitted as a separate document from the F&A rate proposal and should be submitted at the same time as the F&A rate proposal. If the FCPP is not submitted with the F&A rate proposal, the institution should advise the CAS of their intention to submit the FCPP and the timeframe for its submission. The FCPP must contain sufficient detail and supporting documentation to allow the Federal negotiator to make an adequate determination as to the allowability of the projected costs, the reasonableness of the projections and the adequacy of the documentation. The FCPP should include expected increases in facility costs related to new capital assets that are under construction. Assets in the planning stages are not acceptable. Projected costs should be identified by category including building depreciation, capital interest and operating interest. FCPP proposals must identify and include projected increases to the MTDC base for the applicable years. This MTDC base adjustment should be based on the average increase to the MTDC base dollars over the last 5 years. If the base projection is made using another method, a full explanation should be submitted. In addition to the review steps presented below, the guidelines for evaluating the projected costs associated with the new facilities are essentially the same as in the prior sections of this Best Practices Manual.

Facility cost increases based on projected costs should be scrutinized carefully and should be accepted only where construction has started and is reconciled to a contractual time-line. When evaluating FCPPs, offsetting factors that could result in facility cost decreases also need to be considered. These might include (1) the amount of old space being vacated and no longer used for organized research, (2) space that will become fully depreciated, (3) MTDC base increases over the same years as the projected costs and (4) lower utility or maintenance costs related to new more energy efficient buildings. The FCPP must be submitted well before the negotiation to allow a negotiator adequate time to review. Facility cost increases proposed after the CAS rate position has been submitted or during the negotiations will not be accepted under any conditions.

Remember, allowing facility projections to be included in future F&A rates is not a given and it is not a right. The costs must be specifically identified and properly documented. If the institution and the Federal government can not reach an agreement on the facility projection component, either party may elect to reduce the number of years to be included in the current negotiation.

STEPS

1. A summary facility cost projection spreadsheet must be submitted for proposed F&A rate projections. An example of a spreadsheet is included in this section. This spreadsheet is an example of a proposal presentation and by no means represents a negotiated or accepted projected increase. Supplementary information substantiating the projected costs that should be submitted on the spreadsheet include the estimated occupancy dates of the new facilities or remodeled space, the estimated useful lives assigned to the assets, the estimated usage of the space and which academic departments and research protocols will occupy the space. In addition, the negotiator should determine what will happen to the space being vacated, if applicable.
2. The projected costs should be identified by each applicable category such as building depreciation, capital interest and operating interest.
3. The institution should also include projections to their organized research MTDC base corresponding to the years the institution is projecting an increase to the facility costs.

COMMENTS

The facility projections should not be included as part of the base year F&A rate proposal. An FCPP should be submitted at the same time as the F&A rate proposal, but must be a separate document. Determine whether the proposed facility increases are associated with buildings and assets that are still in the planning stages. Major infrastructure or research facility construction and renovation projects must be under construction in order to be considered in the rate negotiation.

Construction must have started and all financing arrangements must be in place. The institution should submit the appropriate contracts and financial arrangements with the FCPP.

The MTDC base increases should be based on the average increase to the MTDC base over the last five (5) years. Any deviation from using the average actual increases should be fully explained.

STEPS

COMMENTS

4. The FCPP should identify the total usable square footage associated with each new facility and the amount of square footage that is being assigned to organized research.

If the facility projections include a significant increase in organized research space, the projected MTDC base should also reflect an increase associated with new researchers joining the institution that may bring new awards and funding opportunities that would not be included in the five year average increase.

Projected facility costs should only be projected into fiscal years where the facilities are expected to be completed and occupied.

Determine how vacated space will be treated. Vacant space should not be classified as organized research. The institution should provide as much detail as possible regarding the expected use of each projected facility. If details by floor or room are not possible, then an estimate for the building is acceptable.

The negotiator should compare the F&A rate base year's organized research MTDC base per organized research square foot to the projected organized research MTDC base per projected organized research square foot (use the total base year plus projected organized research square feet). If the projected MTDC base per projected square foot amount significantly decreases, the reasonableness of the projection may be questioned. Although new facility space may be partially used for decompression, the ratio of the increase in space to the increase in the MTDC base should be comparatively similar.

STEPS

5. Determine if the institution is proposing general "inflation" factors in the FCPP.
6. When an FCPP is submitted, there are many factors that must be considered when deciding the number of years to be negotiated.

COMMENTS

Inflationary factors should not be accepted since inflation affects both the F&A costs pools and the direct cost bases, and should, therefore, not cause an increase in the F&A rates.

If the negotiator feels that there are too many uncertainties regarding the projected facility costs and the MTDC base costs, it may be advantageous to both parties to negotiate the F&A rates for a shorter time period such as one or two years. **Remember**, allowing facility projections to be included in future F&A rates is not a given and it is not a right. The costs must be specifically identified and properly documented. If the institution and the Federal government can not reach an agreement on the facility projection component, either party may elect to reduce the number of years to be included in the current negotiation.

Significant changes to consider in negotiation that may occur after the FCPP submission include:

- a) the occupancy date
- b) the total projected construction costs
- c) the total usable square feet
- d) the square feet assigned to research
- e) the amount of vacant space
- f) the interest rate
- g) the increases to the organized research MTDC base

STEPS

COMMENTS

Increases to the rate should only be accepted where the latest occupancy and use information has been verified and there is clear documented evidence that the facility is under construction.

EXAMPLE OF A FACILITY COST PROJECTION PROPOSAL WORKSHEET

FY-16 OR Base \$58,890,380

Project Name	Yrs.	Est. Use Life / Annual Deprec.	OR				FY 2018 MTDC 8% per year incr.	Rate Eff.	FY 2019 MTDC 8% per year incr.	Rate Eff.	FY 2020 MTDC 8% per year incr.	Rate Eff.
			Sq. Ft.	Instruction Sq. Ft.	Other Sq. Ft.	Total Sq. Ft.						
1 <u>New Chemistry Building</u>			8,000	17,500	2,500	28,000						
Estimated Use			29%	63%	9%	100%						
Construction costs		\$38,000,000										
Capital interest		<u>550,000</u>										
Depreciable costs	40	\$963,750	\$275,357	\$602,344	\$86,049	\$68,689,739	0.40%	\$74,184,918	0.37%	\$80,119,712	0.34%	
Annual interest		750,000	\$214,286	\$468,750	\$66,964	\$68,689,739	0.31%	\$74,184,918	0.29%	\$80,119,712	0.27%	
Total		<u><u>\$39,300,000</u></u>	<u>\$489,643</u>	<u>\$1,071,094</u>	<u>\$153,013</u>		<u>0.71%</u>		<u>0.66%</u>		<u>0.61%</u>	
Estimated Completion	April-17											

