FEDERAL TECHNOLOGY MANAGEMENT POLICY DIVISION
AUTHORITIES RELATED TO THE TECHNOLOGY TRANSFOR PROCESS CHART

"GOVERNMENT RESEARCH ESTABLISHMENTS" -- (GOGOs)

P.L. 96-517 -- Basic invention ownership and Government licensing policies
P.L. 98-620 -- Regulations for licensing Government-owned patents
P.L. 98-622 -- Report on Government use of Statutory Invention Registration
P.L. 96-480 -- Section 5 on innovation, including Stevenson/Wydler report and support of Section 11 on Federal laboratories.
E.O. 10096 -- Policies and operation of Government employee inventor program
H.R. 3773/ S. 1914 -- Model agreements for laboratory/industry collaboration
-- Advice on evaluating commercial potential of inventions
-- Bi-annual report on agency use of provisions

"UNIVERSITIES AND RESEARCH COUNCILS" -- (All Government-funded non-profit R&D organizations including GOCO contractors)

P.L. 96-517 -- Basic policies
Cir. A-124 -- OMB Implementing regulations, lead agency assignment
P.L. 98-620 -- DOC implementing regulations, particularly for GOCOs, statutory lead agency assignment
FAR -- Guide FAR implementation of 98-620
-- Guide FAR implementation of Technical Data

"INVENTOR ENTREPRENEURS" -- (Small business)

P.L. 96-517 -- Basic policies
P.L. 97-219 -- Small Business Innovation Research Program, based on patent policies in 96-517
P.L. 98-620 -- DOC regulations for small business
FAR Technical data provisions

"CONTRACT RESEARCH AND RAs" -- All other R&D contractors

OMB memo delegating DOC as policy lead agency
Presidential Patent Policy Memorandum
FAR -- Uniform provisions for all contractors including for-profit operators of GOCOs
S. 64 -- Coordinate Administration support

"COMPANY LABORATORIES"

P.L. 98-622 -- Study of employeed inventors' rights

"FOREIGN SOURCES" ?

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EXECUTIVE OFFICE OF THE PRESIDENT
OFFICE OF MANAGEMENT AND BUDGET
WASHINGTON, D.C. 20503

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CIRCULAR NO. A-21
Revised

TO THE HEADS OF EXECUTIVE DEPARTMENTS AND ESTABLISHMENTS

SUBJECT: Cost principles for educational institutions

1. Purpose. This Circular establishes principles for determining costs applicable to grants, contracts, and other agreements with educational institutions. The principles deal with the subject of cost determination, and make no attempt to identify the circumstances or dictate the extent of agency and institutional participation in the financing of a particular project. The principles are designed to provide that the Federal Government bear its fair share of total costs, determined in accordance with generally accepted accounting principles, except where restricted or prohibited by law. Agencies are not expected to place additional restrictions on individual items of cost. Provision for profit or other increment above cost is outside the scope of this Circular.

2. Supersession. The Circular supersedes Federal Management Circular 73-8, dated December 19, 1973. FMC 73-8 is revised and reissued under its original designation of OMB Circular No. A-21.

3. Applicability.

a. All Federal agencies that sponsor research and development, training, and other work at educational institutions shall apply the provisions of this Circular in determining the costs incurred for such work. The principles shall also be used as a guide in the pricing of fixed price or lump sum agreements.

b. In addition, Federally Funded Research and Development Centers associated with educational institutions shall be required to comply with the Cost Accounting Standards, rules and regulations issued by the Cost Accounting Standards Board, and set forth in 4 CFR Ch. III;

provided that they are subject thereto under defense related contracts.

4. Responsibilities. The successful application of cost accounting principles requires development of mutual understanding between representatives of educational institutions and of the Federal Government as to their scope, implementation, and interpretation.

5. Attachment. The principles and related policy guides are set forth in the Attachment, "Principles for determining costs applicable to grants, contracts, and other agreements with educational institutions."

6. Effective date. The provisions of this Circular shall be effective October 1, 1979. The provisions shall be implemented by institutions as of the start of their first fiscal year beginning after that date. Earlier implementation, or a delay in implementation of individual provisions, is permitted by mutual agreement between an institution and the cognizant Federal agency.

7. Inquiries. Further information concerning this Circular may be obtained by contacting the Financial Management Branch, Budget Review Division, Office of Management and Budget, Washington, D.C. 20503, telephone (202) 395-6823.

James T. McIntyre, Jr.
James T. McIntyre, Jr.
Director

Attachment

ATTACHMENT
CIRCULAR NO. A-21

PRINCIPLES FOR DETERMINING COSTS APPLICABLE TO GRANTS, CONTRACTS, AND OTHER AGREEMENTS WITH EDUCATIONAL INSTITUTIONS

(No. A-21)

PRINCIPLES FOR DETERMINING COSTS APPLICABLE TO GRANTS, CONTRACTS, AND OTHER AGREEMENTS WITH EDUCATIONAL INSTITUTIONS

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PRINCIPLES FOR DETERMINING COSTS APPLICABLE TO GRANTS, CONTRACTS, AND OTHER AGREEMENTS WITH EDUCATIONAL INSTITUTIONS

A. Purpose and scope.

1. Objectives. This Attachment provides principles for determining the costs applicable to research and development, training, and other sponsored work performed by colleges and universities under grants, contracts, and other agreements with the Federal Government. These agreements are referred to as sponsored agreements.

2. Policy guides. The successful application of these cost accounting principles requires development of mutual understanding between representatives of universities and of the Federal Government as to their scope, implementation, and interpretation. It is recognized that--

a. The arrangements for Federal agency and institutional participation in the financing of a research, training, or other project are properly subject to negotiation between the agency and the institution concerned, in accordance with such Government-wide criteria or legal requirements as may be applicable.

b. Each institution, possessing its own unique combination of staff, facilities, and experience, should be encouraged to conduct research and educational activities in a manner consonant with its own academic philosophies and institutional objectives.

c. The dual role of students engaged in research and the resulting benefits to sponsored agreements are fundamental to the research effort and shall be recognized in the application of these principles.

d. Each institution, in the fulfillment of its obligations, should employ sound management practices.

e. The application of these cost accounting principles should require no significant changes in the generally accepted accounting practices of colleges and universities. However, the accounting practices of individual colleges and universities must support the accumulation of costs as required by the principles, and must provide for adequate documentation to support costs charged to sponsored agreements.

f. Cognizant Federal agencies involved in negotiating indirect cost rates and auditing should assure

that institutions are generally applying these cost accounting principles on a consistent basis. Where wide variations exist in the treatment of a given cost item among institutions, the reasonableness and equitableness of such treatments should be fully considered during the rate negotiations and audit.

3. Application. These principles shall be used in determining the allowable costs of work performed by colleges and universities under sponsored agreements. The principles shall also be used in determining the costs of work performed by such institutions under subgrants, cost-reimbursement subcontracts, and other awards made to them under sponsored agreements. They also shall be used as a guide in the pricing of fixed-price contracts and subcontracts where costs are used in determining the appropriate price. The principles do not apply to:

a. Arrangements under which Federal financing is in the form of loans, scholarships, fellowships, traineeships, or other fixed amounts based on such items as education allowance or published tuition rates and fees of an institution.

b. Capitation awards.

c. Other awards under which the institution is not required to account to the Government for actual costs incurred.

B. Definition of terms.

1. Major functions of an institution refers to instruction (includes departmental research), organized research, other sponsored activities, and other institutional activities as defined below:

a. Instruction means the teaching and training activities of an institution. Except for research training as provided in c below, this term includes all teaching and training activities, whether they are offered for credits toward a degree or certificate or on a noncredit basis, and whether they are offered through regular academic departments or separate divisions, such as a summer school division or an extension division.

b. Departmental research means all research and development activities that are not organized research and, consequently, are not separately budgeted and accounted for.

Departmental research, for purposes of this document, is not considered as a major function of an institution but as a part of the instruction function of the institution.

c. Organized research means all research and development activities of an institution that are separately budgeted and accounted for. This term includes research and development activities that are sponsored by Federal and non-Federal agencies and organizations, as well as those that are separately budgeted by the institution under an internal allocation of institutional funds. It also includes activities involving the training of individuals in research techniques (commonly called research training) where such activities utilize the same facilities as other research and development activities, and where such activities are not included in the instruction function. The costs of organized research and development activities include all costs incurred by the institution in performing the activities.

d. Other sponsored activities means programs and projects financed by Federal and non-Federal agencies and organizations which involve the performance of work other than instruction and organized research. Examples of such programs and projects are health service projects, and community service programs. However, when any of these activities are undertaken by the institution without outside support, they may be classified as other institutional activities.

e. Other institutional activities means all activities of an institution except: (1) instruction, departmental research, organized research, and other sponsored activities, as defined above; (2) indirect cost activities identified in Section F; and (3) specialized service facilities described in Section J38. Other institutional activities include operation of residence halls, dining halls, hospitals and clinics, student unions, intercollegiate athletics, bookstores, faculty housing, student apartments, guest houses, chapels, theaters, public museums, and other similar auxiliary enterprises. This definition also includes any other categories of activities, costs of which are "unallowable" to sponsored agreements, unless otherwise indicated in the agreements.

2. Sponsored agreement, for purposes of this Circular, means any grant, contract, or other agreement between the institution and the Federal Government.

3. Allocation means the process of assigning a cost, or a group of costs, to one or more cost objective, in reasonable and realistic proportion to the benefit provided or other equitable relationship. A cost objective may be a major function of the institution, a particular service or project, a sponsored agreement, or an indirect cost activity, as described in Section F. The process may entail assigning a cost(s) directly to a final cost objective or through one or more intermediate cost objectives.

C. Basic considerations.

1. Composition of total costs. The cost of a sponsored agreement is comprised of the allowable direct costs incident to its performance, plus the allocable portion of the allowable indirect costs of the institution, less applicable credits as described in 5 below.

2. Factors affecting allowability of costs. The tests of allowability of costs under these principles are: (a) they must be reasonable; (b) they must be allocable to sponsored agreements under the principles and methods provided herein; (c) they must be given consistent treatment through application of those generally accepted accounting principles appropriate to the circumstances; and (d) they must conform to any limitations or exclusions set forth in these principles or in the sponsored agreement as to types or amounts of cost items.

3. Reasonable costs. A cost may be considered reasonable if the nature of the goods or services acquired or applied, and the amount involved therefor, reflect the action that a prudent person would have taken under the circumstances prevailing at the time the decision to incur the cost was made. Major considerations involved in the determination of the reasonableness of a cost are: (a) whether or not the cost is of a type generally recognized as necessary for the operation of the institution or the performance of the sponsored agreement; (b) the restraints or requirements imposed by such factors as arm's-length bargaining, Federal and State laws and regulations, and sponsored agreement terms and conditions; (c) whether or not the individuals concerned acted with due prudence in the circumstances, considering their responsibilities to the institution, its employees, its students, the Government, and the public at large; and (d) the extent to which the actions taken with respect to the incurrence of the cost are consistent with established institutional policies and

practices applicable to the work of the institution generally, including sponsored agreements.

4. Allocable costs.

a. A cost is allocable to a particular cost objective (i.e., a specific function, project, sponsored agreement, department, or the like) if the goods or services involved are chargeable or assignable to such cost objective in accordance with relative benefits received or other equitable relationship. Subject to the foregoing, a cost is allocable to a sponsored agreement if (1) it is incurred solely to advance the work under the sponsored agreement; (2) it benefits both the sponsored agreement and other work of the institution, in proportions that can be approximated through use of reasonable methods, or (3) it is necessary to the overall operation of the institution and, in light of the principles provided in this Circular, is deemed to be assignable in part to sponsored projects. Where the purchase of equipment or other capital items is specifically authorized under a sponsored agreement, the amounts thus authorized for such purchases are assignable to the sponsored agreement regardless of the use that may subsequently be made of the equipment or other capital items involved.

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

5. Applicable credits.

a. The term applicable credits refers to those receipts or negative expenditures that operate to offset or reduce direct or indirect cost items. Typical examples of such transactions are: purchase discounts, rebates, or allowances; recoveries or indemnities on losses; and adjustments of overpayments or erroneous charges. This term also includes "educational discounts" on products or services provided specifically to educational institutions, such as discounts on computer equipment, except where the arrangement is clearly and explicitly identified as a gift by the vendor.

b. In some instances, the amounts received from the Federal Government to finance institutional activities or service operations should be treated as applicable credits. Specifically, the concept of netting such credit items against related expenditures should be applied by the institution in determining the rates or amounts to be charged to sponsored agreements for services rendered whenever the facilities or other resources used in providing such services have been financed directly, in whole or in part, by Federal funds. (See Sections F8, J9a, and J38 for areas of potential application in the matter of direct Federal financing.)

6. Costs incurred by State and local governments. Costs incurred or paid by State or local governments on behalf of their colleges and universities for fringe benefit programs such as pension costs and FICA and any other costs specifically incurred on behalf of, and in direct benefit to, the institutions are allowable costs of such institutions whether or not these costs are recorded in the accounting records of the institutions, subject to the following:

a. The costs meet the requirements of C1 through 5 above.

b. The costs are properly supported by cost allocation plans in accordance with applicable Federal cost accounting principles.

c. The costs are not otherwise borne directly or indirectly by the Federal Government.

7. Limitations on allowance of costs. Sponsored agreements may be subject to statutory requirements that limit the allowance of costs. When the maximum amount allowable under a limitation is less than the total amount determined in accordance with the principles in this Circular, the amount not recoverable under a sponsored agreement may not be charged to other sponsored agreements.

D. Direct costs.

1. General. Direct costs are those costs that can be identified specifically with a particular sponsored project, an instructional activity, or any other institutional activity; or that can be directly assigned to such activities relatively easily with a high degree of accuracy.

2. Application to sponsored agreements. Identification with the sponsored work rather than the nature of the goods and services involved is the determining factor in distinguishing direct from indirect costs of sponsored agreements. Typical costs charged directly to a sponsored agreement are the compensation of employees for performance of work under the sponsored agreement, including related fringe benefit costs to the extent they are consistently treated, in like circumstances, by the institution as direct rather than indirect costs; the costs of materials consumed or expended in the performance of the work; and other items of expense incurred for the sponsored agreement, including extraordinary utility consumption. The cost of materials supplied from stock or services rendered by specialized facilities or other institutional service operations may be included as direct costs of sponsored agreements, provided such items are consistently treated, in like circumstances, by the institution as direct rather than indirect costs, and are charged under a recognized method of computing actual costs, and conform to generally accepted cost accounting practices consistently followed by the institution.

E. Indirect costs.

1. General. Indirect costs are those that are incurred for common or joint objectives and therefore cannot be identified readily and specifically with a particular sponsored project, an instructional activity, or any other institutional activity. At educational institutions such costs normally are classified under the following indirect cost categories: depreciation and use allowances, general administration and general expenses, sponsored projects administration expenses, operation and maintenance expenses, library expenses, departmental administration expenses, and student administration and services.

2. Criteria for distribution.

a. Base period. A base period for distribution of indirect costs is the period during which the costs are incurred. The base period normally should coincide with the fiscal year established by the institution, but in any event the base period should be so selected as to avoid inequities in the distribution of costs.

b. Need for cost groupings. The overall objective of the indirect cost allocation process is to distribute the indirect costs described in Section F to the major functions of the institution in proportions reasonably consistent with

the nature and extent of their use of the institution's resources. In order to achieve this objective, it may be necessary to provide for selective distribution by establishing separate groupings of cost within one or more of the indirect cost categories referred to in E1 above. In general, the cost groupings established within a category should constitute, in each case, a pool of those items of expense that are considered to be of like nature in terms of their relative contribution to (or degree of remoteness from) the particular cost objectives to which distribution is appropriate. Cost groupings should be established considering the general guides provided in c below. Each such pool or cost grouping should then be distributed individually to the related cost objectives, using the distribution base or method most appropriate in the light of the guides set forth in d below.

c. General considerations on cost groupings. The extent to which separate cost groupings and selective distribution would be appropriate at an institution is a matter of judgment to be determined on a case-by-case basis. Typical situations which may warrant the establishment of two or more separate cost groupings (based on account classification or analysis) within an indirect cost category include but are not limited to the following:

(1) Where certain items or categories of expense relate solely to one of the major functions of the institution or to less than all functions, such expenses should be set aside as a separate cost grouping for direct assignment or selective allocation in accordance with the guides provided in E2b and d.

(2) Where any types of expense ordinarily treated as general administration or departmental administration are charged to sponsored agreements as direct costs, expenses applicable to other activities of the institution when incurred for the same purposes in like circumstances must, through separate cost groupings, be excluded from the indirect costs allocable to those sponsored agreements and included in the direct cost of other activities for cost allocation purposes.

(3) Where it is determined that certain expenses are for the support of a service unit or facility whose output is susceptible of measurement on a workload or other quantitative basis, such expenses should be set aside as a separate cost grouping for distribution on such basis

to organized research, instructional, and other activities at the institution or within the department.

(4) Where activities provide their own purchasing, personnel administration, building maintenance or similar service, the distribution of general administration and general expenses, or operation and maintenance expenses to such activities should be accomplished through cost groupings which include only that portion of central indirect costs (such as for overall management) which are properly allocable to such activities.

(5) Where the institution elects to treat fringe benefits as indirect charges, such costs should be set aside as a separate cost grouping for selective distribution to related cost objectives.

(6) The number of separate cost groupings within a category should be held within practical limits, after taking into consideration the materiality of the amounts involved and the degree of precision attainable through less selective methods of distribution.

d. Selection of distribution method.

(1) Actual conditions must be taken into account in selecting the method or base to be used in distributing individual cost groupings. The essential consideration in selecting a base is that it be the one best suited for assigning the pool of costs to cost objectives in accordance with benefits derived; a traceable cause and effect relationship; or logic and reason, where neither benefit nor cause and effect relationship is determinable.

(2) Where a cost grouping can be identified directly with the cost objective benefited, it should be assigned to that cost objective.

(3) Where the expenses in a cost grouping are more general in nature, the distribution may be based on a cost analysis study which results in an equitable distribution of the costs. Such cost analysis studies may take into consideration weighting factors, population, or space occupied if appropriate. Cost analysis studies, however, must (a) be appropriately documented in sufficient detail for subsequent review by the cognizant Federal agency, (b) distribute the costs to the related cost objectives in accordance with the relative benefits derived, (c) be statistically sound, (d) be performed specifically at

the institution at which the results are to be used, and (e) be reviewed periodically, but not less frequently than every two years, updated if necessary, and used consistently. Any assumptions made in the study must be stated and explained. The use of cost analysis studies and periodic changes in the method of cost distribution must be fully justified.

(4) If a cost analysis study is not performed, or if the study does not result in an equitable distribution of the costs, the distribution shall be made in accordance with the appropriate base cited in Section F., unless one of the following conditions is met: (a) it can be demonstrated that the use of a different base would result in a more equitable allocation of the costs, or that a more readily available base would not increase the costs charged to sponsored agreements, or (b) the institution qualifies for, and elects to use, the simplified method for computing indirect cost rates described in Section H.

e. Order of Distribution.

(1) Indirect cost categories consist of depreciation and use allowance, operation and maintenance, general administration and general expenses, departmental administration, sponsored projects administration, library, and student administration and services, as described in Section F.

(2) Depreciation and use allowances, operation and maintenance expenses, and general administrative and general expenses should be allocated in that order to the remaining indirect cost categories as well as to the major functions and specialized service facilities of the institution. Other cost categories may be allocated in the order determined to be most appropriate by the institutions. When cross allocation of costs is made as provided in (3) below, this order of allocation does not apply.

(3) Normally an indirect cost category will be considered closed once it has been allocated to other cost objectives, and costs may not be subsequently allocated to it. However, a cross allocation of costs between two or more indirect cost categories may be used if such allocation will result in a more equitable allocation of costs. If a cross allocation is used, an appropriate modification to the composition of the indirect cost categories described in Section F is required.

F. Identification and assignment of indirect costs.

1. Depreciation and use allowances.

a. The expenses under this heading are the portion of the costs of the institution's buildings, capital improvements to land and buildings, and equipment which are computed in accordance with Section J9.

b. In the absence of the alternatives provided for in Section E2d, the expenses included in this category shall be allocated in the following manner:

(1) Depreciation or use allowances on buildings used exclusively in the conduct of a single function, and on capital improvements and equipment used in such buildings, shall be assigned to that function.

(2) Depreciation or use allowances on buildings, used for more than one function, and on capital improvements and equipment used in such buildings, shall be allocated to the individual functions performed in each building on the basis of usable square feet of space, excluding common areas such as hallways, stairwells, and restrooms.

(3) Depreciation or use allowances on buildings and capital improvements where space is used jointly, and on equipment used jointly, shall be allocated to benefiting functions in proportion to the total salaries and wages applicable to the joint functions.

(4) Depreciation or use allowances on buildings, capital improvements, and equipment used predominantly for one function and only incidentally for other(s), may be assigned to the function in which it is used predominantly.

(5) Depreciation or use allowances on certain capital improvements to land, such as paved parking areas, fences, sidewalks, and the like, not included in the cost of buildings, shall be allocated to user categories of students and employees on a full-time equivalent basis. The amount allocated to the student category shall be assigned to the instruction function of the institution. The amount allocated to the employee category shall be further allocated to the major functions of the institution in proportion to the salaries and wages of all employees applicable to those functions.

2. Operation and maintenance expenses.

a. The expenses under this heading are those that have been incurred by a central service organization or at the departmental level for the administration, supervision, operation, maintenance, preservation, and protection of the institution's physical plant. They include expenses normally incurred for such items as janitorial and utility services; repairs and ordinary or normal alterations of buildings, furniture and equipment; and care of grounds and maintenance and operation of buildings and other plant facilities. The operation and maintenance expense category should also include the fringe benefit costs applicable to the salaries and wages included therein, and depreciation and use allowance.

b. In the absence of the alternatives provided for in Section E2d, the expenses included in this category shall be allocated in the same manner as described in Section F1b for depreciation and use allowances.

3. General administration and general expenses.

a. The expenses under this heading are those that have been incurred for the general executive and administrative offices of educational institutions and other expenses of a general character which do not relate solely to any major function of the institution; i.e., solely to (1) instruction, (2) organized research, (3) other sponsored activities, or (4) other institutional activities. The general administration and general expense category should also include the fringe benefit costs applicable to the salaries and wages included therein, an appropriate share of operation and maintenance expense, and depreciation and use allowances.

b. In the absence of the alternatives provided for in Section E2d, the expenses included in this category shall 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 shall then be allocated to serviced or benefited functions on the modified total cost basis. Modified total costs consist of salaries and wages, fringe benefits, materials and supplies, services, travel, and subgrants and subcontracts up to $25,000 each. When an activity included in this indirect cost category provides a service or product to another institution or organization, an appropriate adjustment must

be made to either the expenses or the basis of allocation or both, to assure a proper allocation of costs.

4. Departmental administration expenses.

a. The expenses under this heading 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. Organized research units include such units as institutes, study centers, and research centers. Departmental administration expenses are subject to the following limitations.

(1) Academic deans' offices. Salaries and operating expenses are limited to those attributable to administrative functions.

(2) Academic departments:

(a) The salaries of the heads of academic departments, divisions, and organized research units are limited to amounts attributable to their administrative duties. Salaries of professorial or professional staff, whose appointment or assignment require administrative work that benefits sponsored projects, may also be included to the extent that the portion so charged is clearly and specifically supported as required in Section J6.

(b) Other administrative and supporting expenses incurred within academic departments are allowable provided they are treated consistently in like circumstances. This would include expenses such as the salaries of secretarial and clerical staffs, the salaries of administrative officers and assistants, travel, office supplies, stockrooms, and the like.

(3) Other fringe benefit costs applicable to the salaries and wages included in (1) and (2) above are allowable, as well as an appropriate share of general administration and general expenses, operation and maintenance expenses, and depreciation and/or use allowances.

b. In the absence of the alternatives provided for in Section E2d, the expenses included in this category shall be allocated as follows:

(1) The administrative expenses of the dean's office of each college and school shall be allocated to the academic departments within that college or school on the modified total cost basis.

(2) The administrative expenses of each academic department, and the department's share of the expenses allocated in (1) above shall be allocated to the appropriate functions of the department on the modified total cost basis.

5. Sponsored projects administration.

a. The expenses under this heading are those that have been 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, his assistants, and their 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. The salaries of professorial or professional staff whose appointments or assignments involve the performance of such administrative work may also be included to the extent that the portion so charged to sponsored agreements administration is clearly identified and supported as required by Section J6. This category should also include the fringe benefit costs applicable to the salaries and wages included therein, an appropriate share of general administration and general expenses, the operation and maintenance expenses, and depreciation and use allowance. Appropriate adjustments should be made for services provided to other functions or organizations.

b. In the absence of the alternatives provided for in Section E2d, the expenses included in this category shall be allocated to the major functions of the institution under which the sponsored projects are conducted on the basis of the modified total cost of sponsored projects.

c. An appropriate adjustment shall be made to eliminate any duplicate charges to sponsored agreements when this category includes similar or identical activities as those included in the general administration and general expense category or other indirect cost items, such as accounting, procurement, or personnel administration.

6. Library expenses.

a. The expenses under this heading are those that have been incurred for the operation of the library, including the cost of books and library materials purchased for the library, less any items of library income that qualify as applicable credits under Section C5. The library expense category should also include the fringe benefits applicable to the salaries and wages included therein, an appropriate share of general administration and general expense, operation and maintenance expense, and depreciation and use allowances. Costs incurred in the purchases of rare books (museum-type books) with no value to sponsored agreements should not be allocated to them.

b. In the absence of the alternatives provided for in Section E2d, the expenses included in this category shall be allocated first on the basis of primary categories of users, including students, professional employees, and other users.

(1) The student category shall consist of full-time equivalent students enrolled at the institution, regardless of whether they earn credits toward a degree or certificate.

(2) The professional employee category shall consist of all faculty members and other professional employees of the institution, on a full-time equivalent basis.

(3) The other users category shall consist of all other users of library facilities.

c. Amounts allocated in b above shall be assigned further as follows:

(1) The amount in the student category shall be assigned to the instruction function of the institution.

(2) The amount in the professional employee category shall be assigned to the major functions of the institution in proportion to the salaries and wages of all faculty members and other professional employees applicable to those functions.

(3) The amount in the other users category shall be assigned to the other institutional activities function of the institution.

7. Student administration and services.

a. The expenses under this heading are those that have been incurred for the administration of student affairs and for services to students, including expenses of such activities as deans of students, admissions, registrar, counseling and placement services, student advisers, student health and infirmary services, catalogs, and commencements and convocations. The salaries of members of the academic staff whose academic appointments or assignments involve the performance of such administrative or service work may also be included to the extent that the portion so charged is supported pursuant to Section J6. This expense category also includes the fringe benefit costs applicable to the salaries and wages included therein, an appropriate share of general administration and general expenses, operation and maintenance, and use allowances and/or depreciation.

b. In the absence of the alternatives provided for in Section E2d, the expenses in this category shall be allocated to the instruction function, and subsequently to sponsored agreements in that function.

8. Offset for indirect expenses otherwise provided for by the Government.

a. The items to be accumulated under this heading are the reimbursements and other payments from the Federal Government which are made to the institution to support solely, specifically, and directly, in whole or in part, any of the administrative or service activities described in F1 through 7 above.

b. The items in this group shall be treated as a credit to the affected individual indirect cost category before that category is allocated to benefiting functions.

G. Determination and application of indirect cost rate or rates.

1. Indirect cost pools.

a. Subject to b below, the separate categories of indirect costs allocated to each major function of the institution as prescribed in Section F shall be aggregated and treated as a common pool for that function. The amount in each pool shall be divided by the distribution base described in G2 below to arrive at a single indirect cost

rate for each function. The rate for each function is used to distribute indirect costs to individual sponsored agreements of that function. Since a common pool is established for each major function of the institution, a separate indirect cost rate would be established for each of the major functions described in Section B1 under which sponsored agreements are carried out.

b. In some instances a single rate basis for use across the board on all work within a major function at an institution may not be appropriate. A single rate for research, for example, might not take into account those different environmental factors and other conditions which may affect substantially the indirect costs applicable to a particular segment of research at the institution. A particular segment of research may be that performed under a single sponored agreement or it may consist of research under a group of sponsored agreements performed in a common environment. The environmental factors are not limited to the physical location of the work. Other important factors are the level of the administrative support required, the nature of the facilities or other resources employed, the scientific disciplines or technical skills involved, the organizational arrangements used, or any combination thereof. Where a particular segment of a sponsored agreement is performed within an environment which appears to generate a significantly different level of indirect costs, provision should be made for a separate indirect cost pool applicable to such work. The separate indirect cost pool should be developed during the regular course of the rate determination process and the separate indirect cost rate resulting therefrom should be utilized; provided it is determined that (1) such indirect cost rate differs significantly from that which would have been obtained under a. above, and (2) the volume of work to which such rate would apply is material in relation to other sponsored agreements at the institution.

2. The distribution basis. Indirect costs shall be distributed to applicable sponsored agreements on the basis of modified total direct costs, consisting of salaries and wages, fringe benefits, materials and supplies, services, travel, and subgrants and subcontracts up to $25,000 each. For this purpose, an indirect cost rate should be determined for each of the separate indirect cost pools developed pursuant to G1, above. The rate in each case should be stated as the percentage which the amount of the particular indirect cost pool is of the modified total direct costs identified with such pool. Other bases may be used where it

can be demonstrated that they produce more equitable results.

3. Negotiated lump sum for indirect costs. A negotiated fixed amount in lieu of indirect costs may be appropriate for self-contained, off-campus, or primarily subcontracted activities where the benefits derived from an institution's indirect services cannot be readily determined. Such negotiated indirect costs will be treated as an offset before allocation to instruction, organized research, other sponsored activities, and other institutional activities. The base on which such remaining expenses are allocated should be appropriately adjusted.

4. Predetermined fixed rates for indirect costs. Public Law 87-638 (76 Stat. 437) authorizes the use of predetermined fixed rates in determining the indirect costs applicable under research agreements with educational institutions. The stated objectives of the law are to simplify the administration of cost-type research and development contracts (including grants) with educational institutions, to facilitate the preparation of their budgets, and to permit more expeditious closeout of such contracts when the work is completed. In view of the potential advantages offered by this procedure, consideration should be given to the negotiation of predetermined fixed rates for indirect costs in those situations where the cost experience and other pertinent facts available are deemed sufficient to enable the parties involved to reach an informed judgment as to the probable level of indirect costs during the ensuing accounting period.

5. Negotiated fixed rates and carry-forward provisions. When a fixed rate is negotiated in advance for a fiscal year (or other time period), the over- or under-recovery for that year may be included as an adjustment to the indirect cost for the next rate negotiation. When the rate is negotiated before the carry-forward adjustment is determined, the carry-forward amount may be applied to the next subsequent rate negotiation. When such adjustments are to be made, each fixed rate negotiated in advance for a given period will be computed by applying the expected indirect costs allocable to sponsored agreements for the forecast period plus or minus the carry-forward adjustment (over- or under-recovery) from the prior period, to the forecast distribution base. Unrecovered amounts under lump-sum agreements or cost-sharing provisions of prior years shall not be carried forward for consideration in the new rate

negotiation. There must, however, be an advance understanding in each case between the institution and the cognizant Federal agency as to whether these differences will be considered in the rate negotiation rather than making the determination after the differences are known. Further, institutions electing to use this carry-forward provision may not subsequently change without prior approval of the cognizant Federal agency. In the event that an institution returns to a postdetermined rate, any over- or under-recovery during the period in which negotiated fixed rates and carry-forward provisions were followed will be included in the subsequent postdetermined rates. Where multiple rates are used, the same procedure will be applicable for determining each rate.

H. Simplified method for small institutions.

1. General.

a. Where the total direct cost of work covered by this Circular at an institution does not exceed $3,000,000 in a fiscal year, the use of the simplified procedure described in 2, below, may be used in determining allowable indirect costs. Under this simplified procedure, the institution's most recent annual financial report and immediately available supporting information with salaries and wages segregated from other costs, will be utilized as a basis for determining the indirect cost rate applicable to all sponsored agreements.

b. The simplified procedure should not be used where it produces results which appear inequitable to the Government or the institution. In any such case, indirect costs should be determined through use of the regular procedure.

2. Simplified procedure

a. Establish the total amount of salaries and wages paid to all employees of the institution.

b. Establish an indirect cost pool consisting of the expenditures (exclusive of capital items and other costs specifically identified as unallowable) which customarily are classified under the following titles or their equivalents:

(1) General administration and general expenses (exclusive of costs of student administration and services, student activities, student aid, and scholarships).

(2) Operation and maintenance of physical plant; and depreciation and use allowances; after appropriate adjustment for costs applicable to other institutional activities.

(3) Library.

(4) Department administration expenses, which will be computed as 20 percent of the salaries and expenses of deans and heads of departments.

In those cases where expenditures classified under (1) above have previously been allocated to other institutional activities, they may be included in the indirect cost pool. The total amount of salaries and wages included in the indirect cost pool must be separately identified.

c. Establish a salary and wage distribution base, determined by deducting from the total of salaries and wages as established in a above the amount of salaries and wages included under b above.

d. Establish the indirect cost rate, determined by dividing the amount in the indirect cost pool, b above, by the amount of the distribution base, c above.

e. Apply the indirect cost rate to direct salaries and wages for individual agreements to determine the amount of indirect costs allocable to such agreements.

J. General provisions for selected items of cost.

Sections 1 through 44 below provide principles to be applied in establishing the allowability of certain items involved in determining cost. These principles should apply irrespective of whether a particular item of cost is properly treated as direct cost or indirect cost. Failure to mention a particular item of cost is not intended to imply that it is either allowable or unallowable; rather determination as to allowability in each case should be based on the treatment provided for similar or related items of cost. In case of a discrepancy between the provisions of a specific sponsored agreement and the provisions below, the agreement should govern.

1. Advertising costs.

a. The term advertising costs means the costs of advertising media and corollary administrative costs. Advertising media include magazines, newspapers, radio and television programs, direct mail, exhibits, and the like.

b. The only advertising costs allowable are those which are solely for (1) the recruitment of personnel required for the performance by the institution of obligations arising under the sponsored agreement, when considered in conjunction with all other recruitment costs, as set forth in Section J32; (2) the procurement of goods and services for the performance of the sponsored agreement; (3) the disposal of scrap or surplus materials acquired in the performance of the sponsored agreement except when institutions are reimbursed for disposal costs at a predetermined amount in accordance with Attachment N, OMB Circular No. A-110; or (4) other specific purposes necessary to meet the requirements of the sponsored agreement.

c. Costs of this nature, if incurred for more than one sponsored agreement or for both sponsored work and other work of the institution, are allowable to the extent that the principles in Sections D and E are observed.

2. Bad debts. Any losses, whether actual or estimated, arising from uncollectible accounts and other claims, related collections costs, and related legal costs, are unallowable.

3. Civil defense costs. Civil defense costs are those incurred in planning for, and the protection of life and property against, the possible effects of enemy attack. Reasonable costs of civil defense measures (including costs in excess of normal plant protection costs, first-aid training and supplies, firefighting training, posting of additional exit notices and directions, and other approved civil defense measures) undertaken on the institution's premises pursuant to suggestions or requirements of civil defense authorities are allowable when distributed to all activities of the institution. Capital expenditures for civil defense purposes will not be allowed, but a use allowance or depreciation may be permitted in accordance with provisions set forth in Section J9. Costs of local civil defense projects not on the institution's premises are unallowable.

4. Commencement and convocation costs. Costs incurred for commencements and convocations are unallowable, except as provided for in Section F7.

5. Communication costs. Costs incurred for telephone services, local and long distance telephone calls, telegrams, radiograms, postage and the like, are allowable.

6. Compensation for personal services

a. General. Compensation for personal services covers all amounts paid currently or accrued by the institution for services of employees rendered during the period of performance under sponsored agreements. Such amounts include salaries, wages, and fringe benefits (See Section J15.). These costs are allowable to the extent that the total compensation to individual employees conforms to the established policies of the institution, consistently applied, and provided that the charges for work performed directly on sponsored agreements and for other work allocable as indirect costs are determined and supported as provided below. Charges to sponsored agreements may include reasonable amounts for activities contributing and intimately related to work under the agreements, such as delivering special lectures about specific aspects of the ongoing activity, writing reports and articles, participating in appropriate seminars, consulting with colleagues and graduate students, and attending meetings and conferences. Incidental work (that in excess of normal for the individual), for which supplemental compensation is paid by an institution under institutional policy, need not be included in the payroll distribution systems described below, provided such work and compensation are separately identified and documented in the financial management system of the institution.

b. Payroll distribution. For each organizational unit of an institution, the distribution of salaries and wages of professorial or professional staff (whether charged direct or required to be distributed to more than one activity for purposes of allocating indirect costs) will be based on either a system of monitored workload or a system of personnel activity reports. The latter system will be used for nonprofessional employees whose costs are charged direct or are required to be distributed to more than one activity for purposes of allocating indirect costs. In the use of either method, it is recognized that, because of the nature of work involved in academic institutions, the various and often interrelated activities of professorial

and professional employees frequently cannot be measured with a high degree of precision, that reliance must be placed on reasonably accurate approximations, and that acceptance of a degree of tolerance in measurement is appropriate.

c. Monitored workload. Under this method the distribution of salaries and wages applicable to sponsored agreements is based on budgeted or assigned workload, updated to reflect any significant changes in workload distributions. A monitored workload system used for salaries and wages charged directly or indirectly to sponsored agreements will meet the following standards:

(1) A system of budgeted or assigned workload will be incorporated into the official records of the institution and encompass both sponsored and all other activities on an integrated basis. The system may include the use of subsidiary records.

(2) The system will reasonably reflect workload of employees, accounting for 100 percent of the work for which the employee is compensated and which is required in fulfillment of the employee's obligations to the institution. Because practices vary among institutions and within institutions as to the total activity constituting a full workload -- when expressed in measurable units, such as contact hours in teaching -- the system will be based on a determination for each individual, reflecting the ratio of each of the activities which comprise the total workload of the individual. (But see Section H for treatment of indirect costs under the simplified method for small institutions.)

(3) The system will provide for modification of an individual's salary or salary distribution commensurate with any significant change in the employee's workload or the ratio of activities comprising the total workload. A significant change in an employee's workload shall be considered to include the following as a minimum: when work begins or ends on a sponsored agreement, when a teaching load is materially modified, when additional unanticipated assignments are received or taken away, when an individual begins or ends a sabbatical leave, prolonged sick leave, or leave without pay, etc. Short-term (such as one or two months) fluctuation between workload categories need not be considered as long as the distribution of salaries and wages is reasonable over the longer term such as an academic period. Whenever it is apparent that a change in workload

will occur or has occurred, the change will be documented over the signature of a responsible official and, if significant, entered into the system.

(4) The system will utilize workload categories reflecting activity which is applicable to each sponsored agreement, each indirect cost activity, and each major function of the institution.

(5) At least annually a statement will be signed by the employee, principal investigator, or responsible official, having first hand knowledge of the work stating that salaries and wages charged to sponsored agreements as direct charges, or that salaries and wages charged to both direct and indirect cost categories, or to more than one indirect cost category are reasonable.

(6) The system will provide for independent internal evaluations to insure that it is working effectively.

(7) In the use of this method an institution shall not be required to provide additional support or documentation for the effort actually performed, but is responsible for assuring that the system meets the above standards.

d. Personnel activity reports. Under this system the distribution of salaries and wages will be supported by personnel activity reports as prescribed below.

(1) Personnel activity reports will reflect the distribution of activity expended by each employee covered by the system.

(2) The reports will reflect an after-the-fact reporting of the percentage of activity of each employee. Charges may be made initally on the basis of estimates made before the services are performed, provided that such charges are promptly adjusted if significant differences are indicated by activity reports.

(3) Each report will account for 100 percent of the activity for which the employee is compensated and which is required in fulfillment of the employee's obligations to the institution. The report will reasonably reflect the percentage of activity applicable to each sponsored agreement, each indirect cost category, and each major function of the institution.

(4) To confirm that the distribution of activity represents a reasonable estimate of the work performed by the employee during the period, each report will be signed by the employee or by a responsible official having first hand knowledge of the work performed.

(5) For professorial and professional staff, the reports will be prepared each academic term, but no less frequently than every six months. For other individuals, the reports will be prepared no less frequently than monthly and will coincide with one or more pay periods.

(6) Where the institution uses time cards or other forms of after-the-fact payroll documents as original documentation for payroll and payroll charges, such documents shall qualify as a personnel activity report provided that they are meet the requirements in (1) through (5) above.

e. Salary rates for faculty members.

(1) Salary rates for academic year. Charges for work performed on sponsored agreements by faculty members during the academic year will be based on the individual faculty member's regular compensation for the continuous period which, under the policy of the institution concerned, constitutes the basis of his salary. Charges for work performed on sponsored agreements during all or any portion of such period are allowable at the base salary rate. In no event will charges to sponsored agreements, irrespective of the basis of computation, exceed the proportionate share of the base salary for that period. This principle applies to all members of the faculty at an institution. Since intra-university consulting is assumed to be undertaken as a university obligation requiring no compensation in addition to full-time base salary, the principle also applies to faculty members who function as consultants or otherwise contribute to a sponsored agreement conducted by another faculty member of the same institution. However, in unusual cases where consultation is across departmental lines or involves a separate or remote operation, and the work performed by the consultant is in addition to his regular departmental load, any charges for such work representing extra compensation above the base salary are allowable provided that such consulting arrangements are specifically provided for in the agreement or approved in writing by the sponsoring agency.

(2) Periods outside the academic year.

(a) Except as otherwise specified for teaching activity in (b) below, charges for work performed by faculty members on sponsored agreements during the summer months or other period not included in the base salary period will be determined for each faculty member at a rate not in excess of the base salary divided by the period to which the base salary relates, and will be limited to charges made in accordance with other parts of this section. The base salary period used in computing charges for work performed during the summer months will be the number of months covered by the faculty member's official academic year appointment.

(b) Charges for teaching activities performed by faculty members on sponsored agreements during the summer months or other periods not included in the base salary period will be based on the normal policy of the institution governing compensation to faculty members for teaching assignments during such periods.

(3) Part-time faculty. Charges for work performed on sponsored agreements by faculty members having only part-time appointments will be determined at a rate not in excess of that regularly paid for the part-time assignments; e.g., an institution pays $5,000 to a faculty member for half-time teaching during the academic year. He devoted one-half of his remaining time to a sponsored agreement. Thus, his additional compensation, chargeable by the institution to the agreement, would be one-half of $5,000, or $2,500.

f. Noninstitutional professional activities. Unless an arrangement is specifically authorized by a Federal sponsoring agency, an institution must follow its institution-wide policies and practices concerning the permissible extent of professional services that can be provided outside the institution for noninstitutional compensation. Where such institution-wide policies do not exist or do not adequately define the permissible extent of consulting or other noninstitutional activities undertaken for extra outside pay, the Government may require that the effort of professional staff working on sponsored agreements be allocated between (1) institutional activities, and (2) noninstitutional professional activities. If the sponsoring agency considers the extent of noninstitutional professional effort excessive, appropriate arrangements governing compensation will be negotiated on a case-by-case basis.

7. Contingency provisions. Contributions to a contingency reserve or any similar provision made for events, the occurrence of which cannot be foretold with certainty as to time, intensity, or with an assurance of their happening, are unallowable. (But see also Section J16c.)

8. Deans of faculty and graduate schools. The salaries and expenses of deans of faculty and graduate schools, or their equivalents, and their staffs, are allowable.

9. Depreciation and use allowances. Institutions may be compensated for the use of their buildings, capital improvements, and equipment; provided that they are used, needed in the institutions' activities, and properly allocable to sponsored agreements. Such compensation shall be made by computing either depreciation or use allowance. Use allowances are the means of providing such compensation when depreciation or other equivalent costs are not computed. The allocation for depreciation or use allowance shall be made in accordance with Section F1. Depreciation and use allowances are computed applying the following rules:

a. The computation of depreciation or use allowances shall be based on the acquisition cost of the assets involved. For this purpose, the acquisition cost will exclude (1) the cost of land; (2) any portion of the cost of buildings and equipment borne by or donated by the Government, irrespective of where title was originally vested or where it is presently located; and (3) any portion of the cost of buildings and equipment contributed by or for the institution where law or agreement prohibit recovery. For an asset donated to the institution by a third party, its fair market value at the time of the donation shall be considered as the acquisition cost.

b. In the use of the depreciation method, the following shall be observed:

(1) The period of useful service or useful life established in each case for usable capital assets must take into consideration such factors as type of construction, nature of the equipment, technological developments in the particular area, and the renewal and replacement policies followed for the individual items or classes of assets involved.

(2) The depreciation method used to charge the cost of an asset (or group of assets) to accounting periods shall reflect the pattern of consumption of the asset during its useful life. In the absence of clear evidence indicating that the expected consumption of the asset will be significantly greater in the early portions than in the later portions of its useful life, the straight-line method shall be presumed to be the appropriate method. Depreciation methods once used shall not be changed unless approved in advance by the cognizant Federal agency.

(3) Where the depreciation method is introduced for application to assets for which use allowance was previously charged, the aggregate amount of use allowances and depreciation applicable to such assets must not exceed the total acquisition cost of the assets.

(4) When the depreciation method is used for buildings, a building "shell" may be treated separately from other building components, such as plumbing system and heating and air conditioning system. Each component item may then be depreciated over its estimated useful life. On the other hand, the entire building, including the shell and all components, may be treated as a single asset and depreciated over a single useful life.

(5) Where the depreciation method is used for a particular class of assets, no depreciation may be allowed on any such assets that have outlived their depreciable lives. (But see also c(3), below.)

c. Under the use allowance method, the following shall be observed:

(1) The use allowance for buildings and improvements (including improvements such as paved parking areas, fences, and sidewalks) will be computed at an annual rate not exceeding two percent of acquisition cost. The use allowance for equipment will be computed at an annual rate not exceeding six and two-thirds percent of acquisition cost.

(2) In contrast to the depreciation method, the entire building must be treated as a single asset without separating its "shell" from other building components under the use allowance method. The entire building must be treated as a single asset, and the two-percent use allowance limitation must be applied to all parts of the building. The two-percent limitation, however, need not be applied to

equipment or other assets that are merely attached or fastened to the building but not permanently fixed and are used as furnishings, decorations or for specialized purposes (e.g., dentist chairs and dental treatment units, counters, laboratory benches bolted to the floor, dishwashers, and carpeting). Such equipment and assets will be considered as not being permanently fixed to the building if they can be removed without the need for costly or extensive alterations or repairs to the building to make the space usable for other purposes. Equipment and assets which meet these criteria will be subject to the six and two-thirds percent equipment use allowance.

(3) A reasonable use allowance may be negotiated for any assets that are considered to be fully depreciated, after taking into consideration the amount of depreciation previously charged to the Government, the estimated useful life remaining at the time of negotiation, the effect of any increased maintenance charges, decreased efficiency due to age, and any other factors pertinent to the utilization of the asset for the purpose contemplated.

d. Except as otherwise provided in b and c above, a combination of the depreciation and use allowance methods may not be used, in like circumstances, for a single class of assets (e.g., buildings, office equipment, and computer equipment).

e. Charges for use allowances or depreciation must be supported by adequate property records, and physical inventories must be taken at least once every two years to ensure that the assets exist and are usable, used, and needed. Statistical sampling techniques may be used in taking these inventories. In addition, when the depreciation method is used, adequate depreciation records showing the amount of depreciation taken each period must also be maintained.

10. Donated services and property. The value of donated services and property are not allowable either as a direct or indirect cost, except that depreciation or use allowances on donated assets are permitted in accordance with Section J9a. The value of donated services and property may be used to meet cost sharing or matching requirements, in accordance with OMB Circular No. A-110.

11. Employee morale, health, and welfare costs and credits. The costs of house publications, health or first-aid clinics and/or infirmaries, recreational activities,

employees' counseling services, and other expenses incurred in accordance with the institution's established practice or custom for the improvement of working conditions, employer-employee relations, employee morale, and employee performance, are allowable. Income generated from any of these activities will be credited to the cost thereof unless such income has been irrevocably set over to employee welfare organizations.

12. Entertainment costs. Costs incurred for amusement, social activities, entertainment, and any items relating thereto, such as meals, lodging, rentals, transportation, and gratuities, are unallowable.

13. Equipment and other capital expenditures.

a. For purposes of this paragraph, the following definitions apply:

(1) Equipment means an article of nonexpendable tangible personal property having a useful life of more than two years, and an acquisition cost of $500 or more per unit. However, consistent with institutional policy, lower limits may be established.

(2) Capital expenditure means the cost of the asset including the cost to put it in place. Capital expenditure for equipment, for example, means the net invoice price of the equipment, including the cost of any modifications, attachments, accessories, or auxiliary apparatus necessary to make it usable for the purpose for which it is acquired. Ancillary charges, such as taxes, duty, protective intransit insurance, freight, and installation may be included in, or excluded from, capital expenditure cost in accordance with the institution's regular accounting practices.

(3) Special purpose equipment means equipment which is used only for research, medical, scientific, or other technical activities.

(4) General purpose equipment means equipment, the use of which is not limited only to research, medical, scientific or other technical activities. Examples of general purpose equipment include office equipment and furnishings, air conditioning equipment, reproduction and printing equipment, motor vehicles, and automatic data processing equipment.

b. The following rules of allowability shall apply to equipment and other capital expenditures:

(1) Capital expenditures for general purpose equipment, buildings, and land are unallowable as direct charges, except where approved in advance by the sponsoring agency.

(2) Capital expenditures for special purpose equipment are allowable as direct charges, provided that the acquisition of items having a unit cost of $1,000 or more is approved in advance by the sponsoring agency.

(3) Capital expenditures for improvements to land, buildings, or equipment which materially increase their value or useful life are unallowable as direct charges, except where approved in advance by the sponsoring agency.

(4) Capital expenditures are unallowable as indirect costs. But see Section J9 for allowability of depreciation or use allowance on buildings, capital improvements, and equipment. Also see Section J33 for allowability of rental costs on land, buildings, and equipment.

14. Fines and penalties. Costs resulting from violations of, or failure of the institution to comply with, Federal, State, and local laws and regulations are unallowable, except when incurred as a result of compliance with specific provisions of the sponsored agreement, or instructions in writing from the contracting officer or equivalent.

15. Fringe benefits.

a. Fringe benefits in the form of regular compensation paid to employees during periods of authorized absences from the job, such as for annual leave, sick leave, military leave, and the like, are allowable, provided such costs are distributed to all institutional activities in proportion to the relative amount of time or effort actually devoted by the employees. See Section J35 for treatment of sabbatical leave.

b. Fringe benefits in the form of employer contributions or expenses for social security, employee insurance, workmen's compensation insurance, tuition or remission of tuition for individual employees or their

families and the like are allowable, provided such benefits are granted in accordance with established institutional policies, and are distributed to all institutional activities on an equitable basis. See Section J36b for treatment of tuition remission provided to students.

c. Rules for pension plan costs are as follows:

(1) Costs of the institution's pension plan which are incurred in accordance with the established policies of the institution are allowable, provided (a) such policies meet the test of reasonableness; (b) the methods of cost allocation are equitable for all activities; (c) the amount of pension cost assigned to each fiscal year is determined in accordance with (2) below; and (d) the cost assigned to a given fiscal year is paid or funded for all plan participants within six months after the end of that year.

(2) The amount of pension cost assigned to each fiscal year shall be determined in accordance with generally accepted accounting principles. Institutions may elect to follow the "Cost Accounting Standard for Composition and Measurement of Pension Cost" (4 CFR Part 412).

(3) Premiums paid for pension plan termination insurance pursuant to the Employee Retirement Income Security Act of 1974 (Public Law 93-406) are allowable. Late payment charges on such premiums are unallowable. Excise taxes on accumulated funding deficiencies and prohibited transactions of pension plan fiduciaries imposed under the Employee Retirement Income Security Act are also unallowable.

d. Fringe benefits may be assigned to cost objectives by identifying specific benefits to specific individual employees or by allocating on the basis of the salaries and wages of the employees receiving the benefits. When the allocation method is used, separate allocations must be made to selective groupings of employees, if the costs in relationship to salaries and wages differ significantly for different groups of employees. Also fringe benefits related to institutional salaries and wages treated as direct costs may be treated as direct costs.

16. Insurance and indemnification.

a. Costs of insurance required or approved, and maintained, pursuant to the sponsored agreement, are allowable.

b. Costs of other insurance maintained by the institution in connection with the general conduct of its activities, are allowable subject to the following limitations: (1) types and extent and cost of coverage must be in accordance with sound institutional practice; (2) costs of insurance or of any contributions to any reserve covering the risk of loss of or damage to Government-owned property are unallowable, except to the extent that the Government has specifically required or approved such costs; and (3) costs of insurance on the lives of officers or trustees are unallowable except where such insurance is part of an employee plan which is not unduly restricted.

c. Contributions to a reserve for a self-insurance program are allowable, to the extent that the types of coverage, extent of coverage, and the rates and premiums would have been allowed had insurance been purchased to cover the risks.

d. Actual losses which could have been covered by permissible insurance (whether through purchased insurance or self-insurance) are unallowable, unless expressly provided for in the sponsored agreement, except that costs incurred because of losses not covered under existing deductible clauses for insurance coverage provided in keeping with sound management practice as well as minor losses not covered by insurance, such as spoilage, breakage and disappearance of small hand tools, which occur in the ordinary course of operations, are allowable.

e. Indemnification includes securing the institution against liabilities to third persons and other losses not compensated by insurance or otherwise. The Government is obligated to indemnify the institution only to the extent expressly provided for in the sponsored agreement, except as provided in d above.

17. Interest, fund raising, and investment management costs.

a. Costs incurred for interest on borrowed capital or temporary use of endowment funds, however represented, are unallowable.

b. Costs of organized fund raising, including financial campaigns, endowment drives, solicitation of gifts and bequests, and similar expenses incurred solely to raise capital or obtain contributions, are unallowable.

c. Costs of investment counsel and staff and similar expenses incurred solely to enhance income from investments are unallowable.

d. Costs related to the physical custody and control of monies and securities are allowable.

18. Labor relations costs. Costs incurred in maintaining satisfactory relations between the institution and its employees, including costs of labor management committees, employees' publications, and other related activities, are allowable.

19. Losses on other sponsored agreements or contracts. Any excess of costs over income under any other sponsored agreement or contract of any nature is unallowable. This includes, but is not limited to, the institution's contributed portion by reason of cost-sharing agreements or any under-recoveries through negotiation of flat amounts for indirect costs.

20. Maintenance and repair costs. Costs incurred for necessary maintenance, repair or upkeep of property (including Government property unless otherwise provided for) which neither add to the permanent value of the property nor appreciably prolong its intended life but keep it in an efficient operating condition, are allowable.

21. Material costs. Costs incurred for purchased materials, supplies, and fabricated parts directly or indirectly related to the sponsored agreement, are allowable. Purchases made specifically for the sponsored agreement should be charged thereto at their actual prices after deducting all cash discounts, trade discounts, rebates, and allowances received by the institution. Withdrawals from general stores or stockrooms should be charged at their cost under any recognized method of pricing stores withdrawals conforming to sound accounting practices consistently followed by the institution. Incoming transportation charges are a proper part of material cost. Direct material cost should include only the materials and supplies actually used for the performance of the sponsored agreement, and due credit should be given for any excess materials retained, or returned to vendors. Due credit

should be given for all proceeds or value received for any scrap resulting from work under the sponsored agreement. Where Government-donated or furnished material is used in performing the sponsored agreement, such material will be used without charge.

22. Memberships, subscriptions and professional activity costs.

a. Costs of the institution's membership in civic, business, technical, and professional organizations are allowable.

b. Costs of the institution's subscriptions to civic, business, professional, and technical periodicals are allowable.

c. Costs of meetings and conferences, when the primary purpose is the dissemination of technical information, are allowable. This includes costs of meals, transportation, rental of facilities, and other items incidental to such meetings or conferences.

23. Patent costs. Costs of preparing disclosures, reports, and other documents required by the sponsored agreement, and of searching the art to the extent necessary to make such invention disclosures, are allowable. In accordance with the clauses of the sponsored agreement relating to patents, costs of preparing documents and any other patent costs, in connection with the filing of a patent application where title is conveyed to the Government, are allowable. (See also Section J34.)

24. Plant security costs. Necessary expenses incurred to comply with security requirements, including wages, uniforms and equipment of personnel engaged in plant protection, are allowable.

25. Preagreement costs. Costs incurred prior to the effective date of the sponsored agreement, whether or not they would have been allowable thereunder if incurred after such date, are unallowable unless approved by the sponsoring agency.

26. Professional services costs.

a. Costs of professional services rendered by the members of a particular profession who are not employees of the institution are allowable, subject to b and c below,

when reasonable in relation to the services rendered and when not contingent upon recovery of the costs from the Government. Retainer fees to be allowable must be reasonably supported by evidence of services rendered.

b. Factors to be considered in determining the allowability of costs in a particular case include (1) the past pattern of such costs, particularly in the years prior to the award of sponsored agreements; (2) the impact of sponsored agreements on the institution's total activity; (3) the nature and scope of managerial services expected of the institution's own organizations; and (4) whether the proportion of Government work to the institution's total activity is such as to influence the institution in favor of incurring the cost, particularly where the services rendered are not of a continuing nature and have little relationship to work under sponsored agreements.

c. Costs of legal, accounting, and consulting services, and related costs, incurred in connection with the prosecution of claims against the Government, are unallowable. Costs of legal, accounting and consulting services, and related costs, incurred in connection with patent infringement litigation, are unallowable unless otherwise provided for in the sponsored agreements.

27. Profits and losses on disposition of plant equipment or other capital assets. Profits or losses arising from the sale or exchange of plant, facilities, equipment or other capital assets, including sale or exchange of either short-term or long-term investments, shall not be considered in computing the costs of sponsored agreements except for pension plans as provided in Section J15c. When assets acquired with Federal funds, in part or wholly, are disposed of, the distribution of the proceeds shall be made in accordance with Attachment N, OMB Circular No. A-110.

28. Proposal costs. Proposal costs are the costs of preparing bids or proposals on potential Government and nongovernment sponsored agreements or projects, including the development of data necessary to support the institution's bids or proposals. Proposal costs of the current accounting period of both successful and unsuccessful bids and proposals normally should be treated as indirect costs and allocated currently to all activities of the institution, and no proposal costs of past accounting periods will be allocable to the current period. However, the institution's established practices may be to treat proposal costs by some other recognized method. Regardless

of the method used, the results obtained may be accepted only if found to be reasonable and equitable.

29. Public information services costs. Cost of news releases pertaining to specific research or scientific accomplishment are allowable, when they result from performance of sponsored agreements.

30. Rearrangement and alteration costs. Cost incurred for ordinary or normal rearrangement and alteration of facilities are allowable. Special arrangement and alteration costs incurred specifically for the project are allowable when such work has been approved in advance by the sponsoring agency.

31. Reconversion costs. Costs incurred in the restoration or rehabilitation of the institution's facilities to approximately the same condition existing immediately prior to commencement of a sponsored agreement, fair wear and tear excepted, are allowable.

32. Recruiting costs.

a. Subject to b, c, and d below, and provided that the size of the staff recruited and maintained is in keeping with workload requirements, costs of "help wanted" advertising, operating costs of an employment office necessary to secure and maintain an adequate staff, costs of operating an aptitude and educational testing program, travel costs of employees while engaged in recruiting personnel, travel costs of applicants for interviews for prospective employment, and relocation costs incurred incident to recruitment of new employees, are allowable to the extent that such costs are incurred pursuant to a well managed recruitment program. Where the institution uses employment agencies, costs not in excess of standard commercial rates for such services are allowable.

b. In publications, costs of help wanted advertising that includes color, includes advertising material for other than recruitment purposes, or is excessive in size (taking into consideration recruitment purposes for which intended and normal institutional practices in this respect), are unallowable.

c. Costs of help wanted advertising, special emoluments, fringe benefits, and salary allowances incurred to attract professional personnel from other institutions that do not meet the test of reasonableness or do not

conform with the established practices of the institution, are unallowable.

d. Where relocation costs incurred incident to recruitment of a new employee have been allowed either as an allocable direct or indirect cost, and the newly hired employee resigns for reasons within his control within twelve months after hire, the institution will be required to refund or credit such relocation costs to the Government.

33. Rental cost of buildings and equipment.

a. Rental costs of buildings or equipment are allowable to the extent that the decision to rent or lease is in accord with Section C-3. Rental arrangements should be reviewed periodically to determine if circumstances have changed and other options are available.

b. Rental costs under "sale and lease back" arrangements are allowable only up to the amount that would be allowed if the institution continued to own the property.

c. Rental costs under "less-than-arms-length" leases are allowable only up to the amount that would be allowed if the institution owned the property. For this purpose, a less-than-arms-length lease is one under which one party to the lease agreement is able to control or substantially influence the actions of the other.

d. Where significant rental costs are incurred under leases which create a material equity in the leased property, they are allowable only up to the amount that would be allowed if the institution purchased the property on the date the lease agreement was executed. For this purpose, a material equity in the property exists when the lease:

(1) is noncancelable or is cancelable only upon the occurrence of some remote contingency, and

(2) has one or more of the following characteristics:

(a) Title to the property passes to the institution at some time during or after the lease period.

(b) The term of the lease corresponds substantially to the estimated useful life of the property

(i.e., the period of economic usefulness to the legal owner of the property).

(c) The initial term is less than the useful life of the property and the institution has the option to renew the lease for the remaining useful life at substantially less than fair rental value.

(d) The property was acquired by the leasor to meet the special needs of the institution and will probably be usable only for that purpose and only by the institution.

(e) The institution has the right, during or at the expiration of the lease, to purchase the property at a price which at the inception of the lease appears to be substantially less than the probable fair market value at the time it is permitted to purchase the property (commonly called a lease with a bargain purchase option), except for any discount normally given to educational institutions.

34. Royalties and other costs for use of patents. Royalties on a patent or amortization of the cost of acquiring a patent or invention or rights thereto, necessary for the proper performance of the sponsored agreement and applicable to tasks or processes thereunder, are allowable unless the Government has a license or the right to free use of the patent, the patent has been adjudicated to be invalid or has been administratively determined to be invalid, the patent is considered to be unenforceable, or the patent has expired.

35. Sabbatical leave costs. Costs of leave of absence by employees for performance of graduate work or sabbatical study, travel, or research are allowable provided the institution has a uniform policy on sabbatical leave for persons engaged in instruction and persons engaged in research. Such costs will be allocated on an equitable basis among all related activities of the institution. Where sabbatical leave is included in fringe benefits for which a cost is determined for assessment as a direct charge, the aggregate amount of such assessments applicable to all work of the institution during the base period must be reasonable in relation to the institution's actual experience under its sabbatical leave policy.

36. Scholarships and student aid costs.

a. Costs of scholarships, fellowships, and other programs of student aid are allowable only when the purpose of the sponsored agreement is to provide training to selected participants and the charge is approved by the sponsoring agency. However, tuition remission and other forms of compensation paid as, or in lieu of, wages to students performing necessary work are allowable provided that (1) there is a bonafide employer-employee relationship between the student and the institution for the work performed, (2) the tuition or other payments are reasonable compensation for the work performed and are conditioned explicitly upon the performance of necessary work, and (3) it is the institution's practice to similarly compensate students in nonsponsored as well as sponsored activities.

b. Charges for tuition remission and other forms of compensation paid to students as, or in lieu of, salaries and wages shall be subject to the reporting requirements stipulated in Section J6, and shall be treated as direct or indirect cost in accordance with the actual work being performed. Tuition remission may be charged on an average rate basis.

37. Severance pay.

a. Severance pay is compensation in addition to regular salary and wages which is paid by an institution to employees whose services are being terminated. Costs of severance pay are allowable only to the extent that such payments are required by law, by employer-employee agreement, by established policy that constitutes in effect an implied agreement on the institution's part, or by circumstances of the particular employment.

b. Severance payments that are due to normal recurring turnover and which otherwise meet the conditions of a above may be allowed provided the actual costs of such severance payments are regarded as expenses applicable to the current fiscal year and are equitably distributed among the institution's activities during that period.

c. Severance payments that are due to abnormal or mass terminations are of such conjectural nature that allowability must be determined on a case-by-case basis. However, the Government recognizes its obligation to participate, to the extent of its fair share, in any specific payment.

38. Specialized service facilities.

a. The costs of institutional services involving the use of highly complex or specialized facilities such as electronic computers, wind tunnels, and reactors are allowable, provided the charge for the service meets the conditions of b through d below.

b. The cost of each service normally shall consist of both its direct costs and its allocable share of indirect costs with deductions for appropriate income or Federal financing as described in Section C5.

c. The cost of such institutional services when material in amount will be charged directly to users, including sponsored agreements based on actual use of the services and a schedule of rates that does not discriminate between federally and nonfederally supported activities of the institution, including use by the institution for internal purposes. Charges for the use of specialized facilities should be designed to recover not more than the aggregate cost of the services over a long-term period agreed to by the institution and the congnizant Federal agency. Accordingly, it is not necessary that the rates charged for services be equal to the cost of providing those services during any one fiscal year as long as rates are reviewed periodically for consistency with the long-term plan and adjusted if necessary.

d. Where the costs incurred for such institutional services are not material, they may be allocated as indirect costs. Such arrangements must be agreed to by the institution and the cognizant Federal agency.

e. Where it is in the best interest of the Government and the institution to establish alternative costing arrangements, such arrangements may be worked out with the cognizant Federal agency.

39. Special services costs. Costs incurred for general public relations activities, alumni activities, and similar services, are unallowable.

40. Student activity costs. Costs incurred for intramural activities, student publications, student clubs, and other student activities, are unallowable, unless specifically provided for in the sponsored agreements.

41. Taxes.

a. In general, taxes which the institution is required to pay and which are paid or accrued in accordance with generally accepted accounting principles are allowable. Payments made to local governments in lieu of taxes which are commensurate with the local government services received are allowable, except for (1) taxes from which exemptions are available to the institution directly or which are available to the institution based on an exemption afforded the Government, and in the latter case when the sponsoring agency makes available the necessary exemption certificates; and (2) special assessments on land which represent capital improvements.

b. Any refund of taxes, interest, or penalties, and any payment to the institution of interest thereon, attributable to taxes, interest, or penalties which were allowed as sponsored agreement costs, will be credited or paid to the Government in the manner directed by the Government. However, any interest actually paid or credited to an institution incident to a refund of tax, interest, and penalty will be paid or credited to the Government only to the extent that such interest accrued over the period during which the institution had been reimbursed by the Government for the taxes, interest, and penalties.

42. Transportation costs. Costs incurred for freight, express, cartage, postage, and other transportation services relating either to goods purchased, in process, or delivered, are allowable. When such costs can readily be identified with the items involved, they may be charged directly as transportation costs or added to the cost of such items. Where identification with the materials received cannot readily be made, inbound transportation costs may be charged to the appropriate indirect cost accounts if the institution follows a consistent, equitable procedure in this respect. Outbound freight, if reimbursable under the terms of the sponsored agreement, should be treated as a direct cost.

43. Travel costs.

a. Travel costs are the expenses for transportation, lodging, subsistence, and related items incurred by employees who are in travel status on official business of the institution. Such costs may be charged on an actual basis, on a per diem or mileage basis in lieu of actual costs incurred, or on a combination of the two,

provided the method used is applied to an entire trip and not to selected days of the trip, and results in charges consistent with those normally allowed by the institution in its regular operations.

b. Travel costs are allowable subject to c, d, e, and f below, when they are directly attributable to specific work under a sponsored agreement or are incurred in the normal course of administration of the institution or a department or program thereof.

c. The difference in cost between first-class air accommodations and less than first-class air accommodations is unallowable except when less than first-class air accommodations are not reasonably available to meet necessary mission requirements, such as where less than first-class accommodations would (1) require circuitous routing, (2) require travel during unreasonable hours, (3) greatly increase the duration of the flight, (4) result in additional costs which would offset the transportation savings, or (5) offer accommodations which are not reasonably adequate for the medical needs of the traveler.

d. Costs of personnel movements of a special or mass nature are allowable only when authorized or approved in writing by the sponsoring agency or its authorized representative.

e. Foreign travel costs are allowable only when the travel has received specific prior approval. Each separate foreign trip must be specifically approved. For purposes of this provision, foreign travel is defined as any travel outside of Canada and the United States and its territories and possessions. However, for an organization located outside Canada and the United States and its territories and possessions, foreign travel means travel outside that country.

f. Domestic travel costs are allowable when permitted by the sponsored agreement. Expenditures for such travel will not be allowed if they exceed the amount specified by more than 25% or $500, whichever is greater, except with an advanced approval of the sponsoring agency.

44. Termination costs applicable to sponsored agreements.

a. Termination of sponsored agreements generally gives rise to the incurrence of costs or to the need for

special treatment of costs, which would not have arisen had the agreement not been terminated. Items peculiar to termination are set forth below. They are to be used in conjunction with all other provisions of this Circular in the case of termination.

b. The cost of common items of material reasonably usable on the institution's other work will not be allowable unless the institution submits evidence that it could not retain such items at cost without sustaining a loss. In deciding whether such items are reasonably usable on other work of the institution, consideration should be given to the institution's plans and orders for current and scheduled work. Contemporaneous purchases of common items by the institution will be regarded as evidence that such items are reasonably usable on the institution's other work. Any acceptance of common items as allowable to the terminated portion of the agreement should be limited to the extent that the quantities of such items on hand, in transit, and on order are in excess of the reasonable quantitative requirements of other work.

c. If in a particular case, despite all reasonable efforts by the institution, certain costs cannot be discontinued immediately after the effective date of termination, such costs are generally allowable within the limitations set forth in this Circular, except that any such costs continuing after termination due to the negligent or willful failure of the institution to discontinue such costs will be considered unacceptable.

d. Loss of useful value of special tooling, and special machinery and equipment is generally allowable, provided (1) such special tooling, machinery, or equipment is not reasonably capable of use in the other work of the institution; (2) the interest of the Government is protected by transfer of title or by other means deemed appropriate by the contracting officer or equivalent; and (3) the loss of useful value as to any one terminated agreement is limited to that portion of the acquisition cost which bears the same ratio to the total acquisition cost as the terminated portion of the agreement bears to the entire terminated agreement and other Government agreements for which the special tooling, special machinery, or equipment was acquired.

e. Rental costs under unexpired leases are generally allowable where clearly shown to have been reasonably necessary for the performance of the terminated

agreement, less the residual value of such leases, if (1) the amount of such rental claimed does not exceed the reasonable use value of the property leased for the period of the agreement and such further period as may be reasonable; and (2) the institution makes all reasonable efforts to terminate, assign, settle, or otherwsie reduce the cost of such lease. There also may be included the cost of alterations of such leased property, provided such alterations were necessary for the performance of the agreement, and of reasonable restoration required by the provisions of the lease.

f. Settlement expenses including the following are generally allowable: (1) accounting, legal, clerical, and similar costs reasonably necessary for the preparation and presentation to contracting officers or equivalent of settlement claims and supporting data with respect to the terminated portion of the agreement, and the termination and settlement of subagreements; and (2) reasonable costs for the storage, transportation, protection, and disposition of property provided by the Government or acquired or produced by the institution for the agreement, except when the institution is reimbursed for disposals at a predetermined amount in accorandance with the provisions of Circular No. A-110.

g. Claims under subagreements, including the allocable portion of claims which are common to the agreement and to other work of the institution, are generally allowable.

K. Certification of charges. To assure that expenditures for sponsored agreements are proper and in accordance with the agreement documents and approved project budgets, the annual and/or final fiscal reports or vouchers requesting payment under the agreements will include a certification, signed by an authorized official of the university, which reads essentially as follows: "I certify that all expenditures reported (or payment requested) are for appropriate purposes and in accordance with the provisions of the application and award documents."