



University of California
Office of the President

Vice President-
Research & Graduate Studies

Research Administration Office

Memo Operating Guidance

No. 08-03
February 22, 2008

TO: CONTRACT AND GRANT OFFICERS EXTRAMURAL FUNDS MANAGERS

Subject: Department of Defense (DoD) Cap on Indirect Costs – 35% TC

On November 13, 2007, the Department of Defense (DoD) Appropriations Act, 2008, bill was signed by the President and is now law. (PL110-116) This bill capped the amount of indirect costs the prime contractor can receive under certain DoD contracts, grants, and cooperative agreements to 35% of Total Cost (TC).

Below is guidance on how to implement this new indirect cost rate cap and an excerpt from a DoD memo from the Under Secretary of Defense that was distributed on December 1, 2007 to various military offices.

Indirect Cost Rate Waiver #08R-093 has been approved for this indirect cost rate limitation.

Guidance

Campuses that have a negotiated F&A (facilities & administration) rate of 53.8 percent, or less, will be financially unaffected (i.e., F&A cannot exceed 35 cents for every \$1 expended; therefore a ratio of 35 cents of F&A to 65 cents of direct costs is the conversion ratio to the “standard” F&A rate based on modified total direct costs.) In situations where all direct costs on an award are F&A eligible, 53.8 percent is effectively the F&A rate cap).

Campuses with F&A rates greater than 53.8 percent may be affected on an award-by award basis, depending on the composition of direct costs that are F&A eligible (e.g., salaries, supplies), versus F&A non-eligible (e.g., equipment, fee remission, subawards greater than \$25,000).

Also, the limitation on payment of indirect costs applies to an award entered into at the prime level only and does not flow down to subcontractors.

What DoD awards are affected?

*Note: The addressees above represent the standard distribution of Contract and Grant Memos. Additional addressees, if any, may be added based on the subject of the Memo. See cc's.

- ✓ The DoD cap applies to all FY 2008 Basic Research appropriations obligated by an award to a non-Federal entity or awardee, i.e., procurement contracts, grants, or cooperative agreements, or other agreements/transactions entered into after enactment of the Act (i.e., awards made on or after November 14, 2007).
- ✓ The DoD cap is applicable to "basic research". This includes DoD funds from "Budget Activity 1" (i.e., 6.1 funds). Awards made from DoD budget activities 6.2 (applied research) and 6.3 (development) are not affected.
- ✓ The cap will be applicable to FY09 funds only if the same cap language is included in the FY09 DoD Appropriations Bill.
- ✓ Award continuations made from FY08 DoD funds are not subject to the cap.
- ✓ Expansions (additional new scope of work and budget) to awards issued before 11/14/07 and funded with FY 08 appropriations (6.1) are affected.
- ✓ Congressionally Directed Medical Research Programs (CDMRP) are funded out of two separate DoD budget activities. These programs encompass breast, prostate, and ovarian cancers, neurofibromatosis, military health, and other specified medical research areas. A small portion of CDMRP is funded from Budget Activity 1, and would be subject to the cap. The majority of CDMRP is funded from the DoD "operations and maintenance" account, and these funds are not subject to the cap.

Steps to Take:

- ✓ In the application stage, campuses should use their negotiated rate when developing the budget proposal.
- ✓ Upon award, the awarding agency will be responsible for any adjustments to the budget proposal. In those situations where the budget proposal included F&A costs that exceeded the cap, the agency may adjust the award, accordingly.
- ✓ In situations where the award was not adjusted, the campus will still be responsible for managing the cap. Subsequently, the campus may rebudget F&A costs in excess of the cap to an allowable direct cost category.
- ✓ To date, awards have been issued with the cap language included as a term or condition of the award. We recommend that you carefully review DoD award notices to confirm any terms or conditions associated with the cap. In the case of the CDMRP, this is particularly important since a small portion of these programs (those awards funded from Budget Activity 1) will be subject to the cap.
- ✓ As specified in the DoD internal guidance (see excerpt below), the cap is applicable to the prime award recipient only, and does not flow down to subrecipients.

- ✓ Finally, campuses must have a system in place to monitor charges, on an award-by-award basis, to ensure the 35 percent cap is not exceeded.

Example:

On a \$100,000 award, \$35,000 in indirects is the maximum allowed ($\$100,000 \times 35\%$).

If \$35,000 is the indirect cost, \$65,000 is the direct cost ($\$100,000 - \$35,000 = \$65,000$)

So, $\$35,000 / \$65,000 = 53.846\%$

Thus, 35% TC = 53.846% of Direct Costs

So, if you have a project with direct costs of \$60,000 (all subject to F&A), and multiply it by 53.846%, then \$32,307 is the maximum indirect costs allowed:

$\$60,000 \times 53.846\% = \$32,307$

Direct Cost	\$60,000
Indirect Cost	<u>\$32,307</u>
Total	\$92,307

$32,307 / 92,307 = 35\%$

Please contact me if you have any questions on this new requirement.

Kathleen P. Babcock, J.D.
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Attachment: Excerpt of Internal Memo from DoD Under Secretary of Defense

cc: Jorge Ohy, CP&A, UCOP

Excerpt of Internal Memo From DoD Under Secretary of Defense:

SUBJECT: Indirect Cost Limitation for Basic Research Awards

Please expeditiously issue direction to all offices or laboratories within your Military Department or Defense Agency that may obligate or transfer for obligation Basic Research appropriations, to require compliance with the requirements of Section 8115 of the DoD Appropriations Act, 2008.

Section 8115 reads:

SEC. 8115. Notwithstanding any other provision of law, none of the funds made available in this Act may be used to pay negotiated indirect cost rates on a contract, grant, or cooperative agreement (or similar arrangement) entered into by the Department of Defense and an entity in excess of 35 percent of the total cost of the contract, grant, or agreement (or similar arrangement): Provided, That this limitation shall apply only to contracts, grants, or cooperative agreements entered into after the date of the enactment of this Act using funds made available in this Act for fiscal year 2008 for basic research.

For the purposes of implementing Section 8115:

- Basic Research means funds in programs within Budget Activity I of the Research, Development, Test and Evaluation appropriation.
- The restriction on payment of indirect costs applies to all FY 2008 Basic Research appropriations obligated by any award - i.e., procurement contract, grant, cooperative agreement, or any other obligational arrangement - to a non-Federal entity, or awardee.
- The limitation on payment of indirect costs applies to an award entered into at the prime level only and does not flow down to subordinate instruments.
- For the restriction on payment of indirect cost as a percentage of total cost, "total cost" has the meaning given in the Government-wide cost principles that apply to the particular awardee (2 CFR part 220, 225, or 230, or 48 CFR part 31). "Indirect costs" are all costs of a prime award that are Facilities and Administration costs (for awardees subject to the cost principles in 2 CFR part 220) or indirect costs (for awardees subject to the cost principles in 2 CFR part 225 or 230 or 48 CFR part 31).

Please issue direction immediately to affected program and awarding offices to include a:

- Term or condition requiring compliance with Section 8115 in each new award made on or after November 14, 2007, using Basic Research funds made available by the DoD Appropriations Act for FY 2008. Section 8115 does not apply to obligations of FY 2008 funds for awards made before that date.

- Statement requiring compliance with Section 8115 in any document transferring FY 2008 Basic Research funds to another Federal agency for obligation to a non-Federal entity. The statement must require the other agency to include a term or condition, as described in the preceding paragraph, in each new award it makes using those funds.