

FY 2008 DoD Appropriation Act 35% Limitation on Payment of Indirect Costs

Section 8115 of the Fiscal Year 2008 Department of Defense Appropriation Act placed a 35% limit on payment of indirect costs under contracts, grants, cooperative agreements and similar agreements awarded using FY 2008 basic research (6.1) funds. The limitation applies only to awards entered into after the date of enactment of the Act (14 November 2007) using FY 08 funds provided by the Act.

The following is provided as clarification to Program Officers, Contracting Officers and Grant Officers to guide their interactions with potential awardees that may be impacted by Section 8115 of the Act.

By memorandum dated 1 December 2007, the Undersecretary of Defense (AT&L) issued guidance on implementation of the Act. The following are the key elements of that guidance with regard to ONR's implementation:

- The limitation on payment of indirect costs applies to all types of 6.1 funded awards, i.e., contracts, grants, cooperative agreements, etc. to any non-Federal entity or awardee. For ONR this means universities, both large and small commercial firms and other non-profit organizations are potentially impacted.
- The limitation on payment of indirect costs applies to prime awards only and **does not** flow down to subcontracts or subgrants.
- The limitation applies to "new" awards funded by FY08 basic research funds. For ONR this means new awards and expansions to existing awards if the new award or expansion is issued on or after 14 November 2007.
- A provision must be placed in each new award using FY 08 basic research funds issued on or after 14 November 2007 requiring compliance with Section 8115 of the DoD Appropriation Act for FY08. ONR Acquisition developed a set of provisions for contracts, grants, etc. meeting these criteria.

The 35% limit on payment of indirect costs is not an indirect cost rate. Instead, it is a limit on the ratio of indirect costs to the total cost of an award; e.g. 35 cents on a dollar. Thus, by dividing the total indirect costs by the total amount of the award we can determine whether the 35% limitation is breached.

Indirect cost rates are negotiated by the government with contractors, grantees and other non-Federal performers who receive funds from the government. The indirect cost rate is a methodology for allocating allowable costs that cannot be readily estimated and charged directly to Federal and non-Federal awards.

University indirect cost rates (referred to as Facility and Administrative rates by regulation) are applied to a restricted set of direct costs (referred to as Modified Total Direct Costs or MTDC) to arrive at the dollar amount of indirect cost applicable to a specific contract, grant or agreement. Included in the MTDC are salaries and wages, fringe benefits, materials and supplies, travel and the first \$25K of each subgrant of subcontract. Excluded from the MTDC are equipment, capital expenditures, tuition remission (paid to graduate research assistants in lieu of salary), rental costs, scholarships and fellowships, patient care costs and the portion of each subgrant of subcontract in excess of \$25K. Bottom line, if a university cost proposal contains more MTDC exclusions there is less likelihood of exceeding the 35% limitation despite the fact that the negotiated indirect cost rate may be substantially higher than 35%.

Indirect cost rates for commercial firms and other non-profit organizations are substantially different in how they are applied. The total amount of indirect costs for a commercial concern or other non-profit organization may consist elements referred to as indirect costs or overhead, general and administrative costs, material overhead, subcontract overhead, etc. or any combination of the above. The BD25 will ultimately determine whether the total amount of indirect cost beaches the limitation. In some cases, the ONR Indirect Cost Branch, BD242, and or the Defense Contract Auditor Agency may be consulted in determining the total amount of indirect costs being proposed. Program Officers are encouraged to contact the Contracting Officer or Grants Officer if questions arise regarding the limitation on payment of indirect costs.