Why are university budgets broken into direct and indirect costs?

Universities in the U.S. are required to follow an accounting methodology established in the Code of Federal Regulations (2 CFR 200, Appendix III).

Direct costs include project-specific line items (salaries, supplies, etc.) **Indirect costs** support sponsored activity in general (e.g., the cost of electricity used in research facilities).

The Federal government mandates the use of indirect cost accounting to avoid unwieldy alternatives. For example, attempting to measure the amount of electricity used on each sponsored project would require extensive accounting, which in turn would drive F&A rates higher.

FY21 Research Rate (Fixed)	On-Campus	Off-Campus
General Administration	7.51%	7.51%
Sponsored Program Administration	13.54%	13.54%
Departmental Administration	7.74%	7.74%
Departmental Admin Allowance	3.60%	3.60%
Administrative Total	**32.39%**	**32.39%**
-Reduction to 26% Cap	-6.39%	-6.39%
Administrative Total (capped)	**26.00%**	**26.0%**
Physical Plant	17.16%	0.0%
Interest	1.19%	0.0%
Library	0.66%	0.0%
Building Depreciation	10.56%	0.0%
Equipment Depreciation	4.37%	0.0%
Facilities Total	**33.94%**	**0.0%**
Carry forward	0.56%	0.0%
Total	**60.50%**	**26%**

The above represent the proposed cost components of the most commonly used F&A rates at Penn State (on- and off-campus research rates.) Separate rates exist for instruction, DoD contract research, college of Medicine research, and research performed at the Applied Research Lab. Complete up-to-date rates can be found at: **research.psu.edu/rates.**

Where can I find up-to-date rates?

Current rates can be found online at:

research.psu.edu/rates

This page also includes a breakdown of the cost components of Penn State's fringe and F&A rates.

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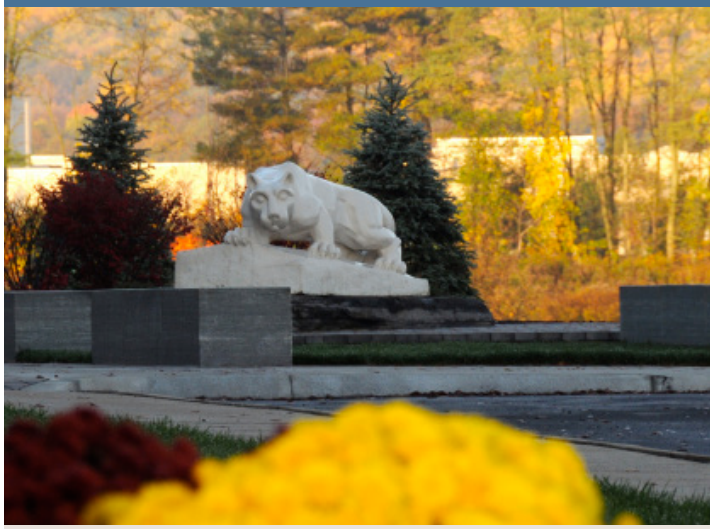
PennState
Senior Vice President for Research

Facilities & Administrative Costs

2021 Quick Guide



Office of Sponsored Programs

The Office of Sponsored Programs provides central coordination and oversight of all research awards that come into Penn State.

For questions about a specific proposal or award, please contact your college research coordinator: **research.psu.edu/coordinators**

For questions related to ongoing contract negotiations, please contact your assigned negotiator: **research.psu.edu/negotiators**

Web: research.psu.edu/osp
Phone: 814-865-1372
Email: osp@psu.edu

How are F&A rates calculated?

A space survey is conducted to determine which facilities are associated with research, which with instruction, and which with other activities.

- Facilities costs include "depreciation on buildings, equipment and capital improvement, interest on debt associated with certain buildings, equipment and capital improvements, and operations and maintenance expenses" (2 CFR 200.414).

- Administrative costs include costs associated with proposal preparation, accounting, invoicing, auditing, federal reporting, and compliance (e.g., human subjects, animal subjects, conflict of interest, research integrity, export control, and data security).

In order to calculate the on-campus research rate, the total costs associated with research facilities and administration are divided by the total direct costs associated with sponsored research (minus certain exclusions). The resultant percentage is Penn State's on-campus research F&A rate. The off-campus research rate is calculated the same way, excluding facilities costs. Penn State's rate calculations are scrutinized by the Office of Naval Research (ONR), Penn State's cognizant federal agency.

When is it appropriate to use the off-campus F&A rate?

Penn State does not break projects into on-campus and off-campus components. If a majority of the salaries and wages (including Penn State cost-share, excluding subrecipients) are incurred on-campus, then the on-campus rate will apply to the entire project. If a majority of such costs are incurred off-campus, then the off-campus rate will apply to the entire project. This policy is articulated in RA30. Specific examples can be found in Q4 of the F&A FAQ.

What if my sponsor says that they won't cover F&A? Can it be waived?

Some exceptions to full F&A recovery are articulated in RA30. Additional detail can be found in Q1-Q3 of the F&A FAQ. In general, the Federal government expects us to recover F&A when we can, especially when working with private industry and foreign governments.

The Federal government's position is that revenue raised via the federally negotiated F&A rate should not be used to subsidize research performed for private companies and foreign governments (2 CFR 200, Appendix III, C.1.a.(3))

What are Research Incentive Funds (RIF)?

A dollar amount equivalent to 12% of recovered F&A is distributed to colleges each year. The colleges are free to spend the funds to support college-level research expenses (e.g., strategic investments in early-stage faculty research).

Alternatively, the colleges can distribute some or all of the RIF to departments, which in turn can distribute some or all of the RIF to faculty members. Faculty members can use the funds to support research-related expenses for which they have no other funding.

Why can't RIF be higher?

RIF could be set at any level. Some universities distribute a dollar amount to their colleges equivalent to 100% of recovered F&A. However, such universities must then distribute the expenses associated with facilities and administration back to the individual colleges. Under such a model, individual colleges would be "billed" for their share of central administrative services and facilities maintenance. Increasing the RIF percentage would neither increase revenue nor decrease expenses.

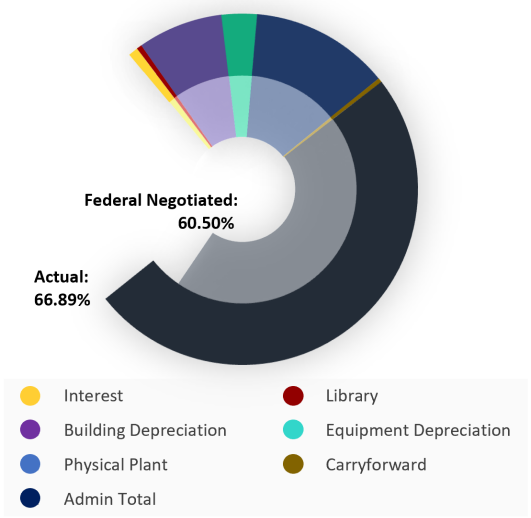
Are there things Penn State could do to reduce its F&A rates?

All universities are concerned that if their rates are too high, their proposals will be considered less competitive. The most obvious way to reduce F&A rates would be to spend less on facilities. If Penn State were to spend less on building, refurbishing, and maintaining research facilities, the facilities portion of its F&A rate would go down. (Of course, excessive neglect of our facilities also would diminish our competitiveness as a research university.)

Decreasing the administrative portion of Penn State's F&A rate is more difficult. Administrative costs are capped at 26% (2 CFR 200, Appendix III, C.8). Most R1 universities, including Penn State, have administrative costs in excess of 26%, thus modest reductions in services would have no impact on the overall rate. It is unlikely that Penn State could cut services enough to bring administrative costs below the cap, since many of these activities are mandated by federal regulation (e.g., audit and compliance requirements).

Actual vs. Negotiated F&A Costs

(On-Campus FY21)



Administrative Cost Breakdown

FY21

General Admin (e.g., institution-wide financial management, personnel management, safety and risk management, general counsel, central IT services) **= 7.51%**

Sponsored Program Admin (e.g., grant and contract administration, special security, purchasing, stock rooms, print shops) = **13.54%**

Department Admin (e.g., deans' offices, academic departments and divisions, institutes, study centers, and research centers) = **11.34%**

TOTAL = 32.39%

The above represent proposed rate components of the FY21 rate.