What happens to F&A cost recovery that is associated with research grants and how is it used?

Introduction

This document emerged from a University initiative to study and improve current practices for assigning F&A cost recoveries (facilities and administrative costs, formerly referred to as indirect costs, indirect cost recoveries, or overhead). The primary aim of the initiative is to enhance collaborative research ventures between investigators in different departments, centers, schools and the two campuses. We hope that improved understanding and transparency of the F&A recovery guidelines and practices will, in part, lead to an even more interactive and productive community of researchers.

Research at Northwestern has increased tremendously, as expenditures for externally sponsored projects have nearly doubled in the last 10 years:

<table>
<thead>
<tr>
<th>Expenditures by Fiscal Year</th>
<th>Direct</th>
<th>F&amp;A Recovery</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>FY1999</td>
<td>$152.9M</td>
<td>$41.0M</td>
<td>$193.9M</td>
</tr>
<tr>
<td>FY2008</td>
<td>$290.6M</td>
<td>$80.0M</td>
<td>$370.6M</td>
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As Northwestern research continues to grow, the underlying structures and processes must also evolve. We have created a standard policy for the assignment of F&A recovery on multi-investigator grants to decrease administrative burden and enable a greater focus on research. As a companion to the standard policy the intention of this FAQs document is to explain concisely what F&A recovery is and how it is used.

Overview

1. Northwestern University does not generate a surplus from its research activities. F&A costs are recovered at a rate and an amount lower than the University’s actual incurred cost of doing research. Research infrastructure and administrative personnel on both the Evanston and Chicago campuses are subsidized by the University due to the lack of full recovery from sponsors. F&A is recovered at a rate lower than both the University’s actual cost of doing research and the rate negotiated with funding agencies.

2. The University uses F&A recovery, about 6% of total annual University revenue ($1.5 billion), in two ways:
   - The F&A recovery generated by research in the Evanston schools is retained centrally to support the budgets of the Evanston schools and central administration.
The F&A recovery generated by research expenditures in the Feinberg School of Medicine, Kellogg School of Management and Northwestern University School of Law is retained fully by each school to partially support their space and administrative expenses, including school administrative costs and each school’s share of University space and administrative costs for services directly used or directly benefitting the schools. (Such costs are not similarly charged to Evanston schools.)

3. Understanding how F&A recovery is treated is important to schools, departments, and centers because a portion of F&A recovery is returned to the schools and Office for Research (in the case of University Research Centers), either directly or indirectly through the annual budget.

Following are FAQ’s to facilitate communication and understanding of the F&A recovery process and policies:

Most federal grants, and some grants funded from other sources such as corporations and foundations, provide two sources of support for organized research: 1) direct funding of costs that are available for the investigators to spend and 2) support for F&A costs that the University incurs and cannot be directly assigned to the award.

#1 – What are direct costs?
The funds available to a principal investigator (PI) upon receipt of a grant, which the PI has outlined in a proposal that are necessary to accomplish the research, and can be directly assigned, are allocable (proportional to the benefit received by the grant) and auditable (requiring validation). These can include postdoctoral research salaries, chemicals, lab gases, and test tubes.

#2 – What are F&A (facilities and administrative) costs?
F&A costs are costs that cannot be directly charged to grants, usually because it not possible to associate those costs with a specific grant (such as utilities, maintenance, building and equipment depreciation, and administrative services).

#3 – What is a negotiated F&A recovery rate?
The percent of direct costs that an agency agrees to pay for F&A costs. For example, currently the negotiated rate for federal agency grants to Northwestern is 52.5%; thus for an NIH grant with $250,000 in direct costs to an investigator, the University receives up to $131,250 in F&A recovery (with a total award of $381,250).

<table>
<thead>
<tr>
<th>Total award</th>
<th>$381,250</th>
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<tbody>
<tr>
<td>Direct cost</td>
<td>$250,000</td>
</tr>
<tr>
<td>Indirect cost</td>
<td>$131,250</td>
</tr>
</tbody>
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#4 – How are negotiated F&A rates determined?
The F&A rate is calculated and negotiated every three to four years with the federal government. A proposal is prepared, according to federally mandated guidelines, based on financial information from a previously agreed upon fiscal year. The proposal is submitted and due to the federal government six months after the end of that year. After submission, the government will typically have questions and request additional data along with back-up documentation. As part of the process, the government will conduct the negotiations on-site with a detailed inspection of Northwestern’s financial records and space information, in addition to interviewing various staff and faculty. There is no obligation by the federal government to fund all costs as proposed. As noted above, invariably, the negotiated rate is less than the proposed rate. Once the rate is finalized, a rate agreement is published and available to all Northwestern constituents. There are different F&A rates for federal projects and non-federal projects, depending upon the type of institutionally sponsored activity.

The final rate is based upon a number of factors. It may increase if:
- Amount of space devoted to organized research increases (either due to new building space or new analysis);
- Utility costs increase for electricity, gas, water, etc.;
- Expensive scientific equipment is purchased with non-sponsored funds.

It may decrease if:
- Amount of space devoted to organized research decreases (researchers funded more through non-sponsored funds);
- Direct expenses increase without a parallel increase in F&A, for example the stimulus funding (ARRA) increases expenses without a proportionate increase in space.

More details on F&A rates may be found in the F&A Primer.

Once an award is accepted by the University, it is set up in Northwestern’s financial system, and as direct costs are incurred, the financial system calculates the F&A costs based upon the applicable negotiated rate.

#5 – How is F&A recovery managed at Northwestern?
Although Northwestern must use some of its F&A recovery, as described in the federal guidance articulated in OMB Circular A-21, to improve research facilities, the University is given discretion in how to use remaining F&A recovery. It is expected that F&A recovery will be used for expenses directly or indirectly related to the conduct of sponsored research. Although the way these funds are used is not usually identified with a particular project or activity, the support this revenue source provides is required for the general operation of the University and the conduct of sponsored activities.

Facilities costs supported by F&A recovery are comprised of building and equipment depreciation, interest from debt financing, operation and maintenance costs and all costs associated with running Northwestern libraries.
Administrative costs supported by F&A include:

- Administrative support staff, such as PI administrative assistants, financial assistants and accounting clerks who are assigned to assist principal investigators in managing their sponsored project activity. These staff members can be serving in the dean’s office, in the department or center office, in an individual laboratory office, and/or in an Office for Research office.
- General material and service costs such as office supplies, copying, postage, and recurring telephone and data line costs that support sponsored project activity, but cannot be charged as direct costs to specific project accounts.
- Central units in support of research such as the Office for Research, Financial Operations, Cost Studies, Accounting Services for Research and Sponsored Programs, Office of General Counsel, and Human Resources.

Source: Office for Research’s website: http://www.research.northwestern.edu/policies/cost-recovery.html

#6 – Are there surplus funds generated from F&A recovery?
No, the University does not generate a funding surplus from research.

#7 – How is it possible that F&A recovery does not generate a funding surplus for the University?
The actual cost of supporting research is greater than the F&A recovery that Northwestern receives. In fiscal year 2008 (2007-08), Northwestern brought in over $290 million in direct costs and about $80 million in F&A recovery, a 27.5% actual F&A recovery rate (see Table below). This actual recovery rate was significantly less than the 51% negotiated F&A recovery rate for federal agencies for this year. The lower recovery rate can occur when cost sharing is used or when specific types of grants are awarded. Some grants, such as training grants, clinical grants, or those from private foundations, allow little or no F&A recovery.

<table>
<thead>
<tr>
<th>Fiscal Year 2008</th>
<th>F&amp;A Recovery Rates Applied to FY 2008</th>
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<tbody>
<tr>
<td>Total Direct Costs</td>
<td>$290,599,910</td>
</tr>
<tr>
<td>Total F&amp;A recovery</td>
<td>$79,978,677</td>
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</tbody>
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The table below lists the actual costs covered by the F&A recovery and illustrates the components of the F&A rate of 52.5% for 2009-2010.

<table>
<thead>
<tr>
<th>Components of Negotiated F&amp;A Rate:</th>
<th>FY 2009</th>
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<tbody>
<tr>
<td>Building Use/Depreciation</td>
<td>6.60%</td>
</tr>
<tr>
<td>Equipment Use/Depreciation</td>
<td>3.20%</td>
</tr>
<tr>
<td>Interest</td>
<td>2.60%</td>
</tr>
<tr>
<td>Operations &amp; Maintenance</td>
<td>11.00%</td>
</tr>
<tr>
<td>Library</td>
<td>1.80%</td>
</tr>
<tr>
<td>Administration</td>
<td>26.00%</td>
</tr>
<tr>
<td>Utility Adjustment</td>
<td>1.30%</td>
</tr>
<tr>
<td>Total</td>
<td><strong>52.50%</strong></td>
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</table>
#8 – *Does the Feinberg School of Medicine generate surplus funds from research?*

No, the F&A recovery FSM receives does not cover the school’s research infrastructure costs.

Different understandings of the University’s central budgeting and FSM’s budget model have led to some lack of clarity about the allocation and use of income from research.

We discussed earlier in the document how central F&A recovery is allocated. As stated in the overview, FSM receives 100% of the F&A recovery it generates and is responsible for covering all of its operating costs including University charges for space and administrative support. F&A recovery comprises about 13% of the total FSM budget and is just one element of FSM’s income. F&A recovery does not generate a net surplus for the school but rather is used in part to fund the University’s support of FSM and other parts of the school’s expenses.

The use of F&A recovery in FSM is described in more detail below:

- In 2008-09 FSM generated $51 million in F&A recovery.
- Within FSM, the dean’s office receives 40% of F&A recovery to cover a portion of operating expenses; 60% of the F&A recovery is assigned directly to departments.
- FSM departments are responsible for all operating and maintenance costs of space and use these funds in part to pay for these costs.
- FSM is a large consumer of space and central administrative and research services. In the same year, FSM reimbursed $75.2 million to the University for:
  - Space and shared services costs (e.g., President’s Office, Provost’s Office, Financial Operations, University Services, Office for Research, etc.)
  - CCM (Center for Comparative Medicine, our animal research laboratories)
  - Enterprise systems projects (Project Café)
  - IT internet and telephone connectivity
- FSM must also allocate a share from other revenue sources (tuition, endowment, gift, clinical affiliates, and parking revenue) to support these costs and other parts of the FSM dean’s office budget (FSM academic and program support, library, recruitment, capital requirements, recruitment commitments, administrative units, financial aid, medical education pool, basic science faculty salaries, and debt service).

*Source: Feinberg School of Medicine Dean’s Office*

#9 – *Do the Evanston schools and the Office for Research generate a surplus from research?*

No, neither the schools nor the Office for Research generate a surplus from research.
#10 – Is the Office for Research’s F&A recovery sharing model different from that of the Evanston schools?

The Office for Research operates on the same F&A recovery-sharing model as the participating Evanston schools.

McCormick, Weinberg, and the University Research Centers all participate in the F&A Recovery Sharing Program in which the participating schools/units receive a portion of the F&A recovery that they generate. The program works as follows: 100% of F&A recovery brought in by grants administered through these units are treated as revenue for the University. The schools or Office for Research (for grants in University Research Centers) then receive 28% of the total F&A recovery generated within their units based on a three-year average as part of their annual allocation. It should be noted that due to federal costing regulations and practices, the amount of F&A the University receives does not fully cover the facilities and administrative costs incurred as a result of sponsored research.

The School of Communication and School of Education and Social Policy currently do not participate in the F&A Recovery Sharing Program and support for their research administrative infrastructure is included in their budget allocation.

**Evanston Schools**

The Office of Budget and Planning appropriates funds to the schools to provide administrative support needed for externally funded research. These funds are used for salaries and benefits for financial/research/administrative staff in the departments, but do not cover the total cost of the staff who support research. For Evanston schools participating in the F&A Recovery Sharing Program, the appropriation is directly tied to the F&A recovery generated by grants that run through each school (see above).

While most of the F&A recovery a school/unit receives is included in its annual allocation, if the amount of F&A recovery generated exceeds the previous year’s amount, the school receives a supplement. The supplements may be used for faculty start-up funds, matching funds, bridge funds, and other commitments related to research. If the amount of F&A recovery generated decreases, then the school must determine whether it wants to make up the difference or adjust spending.

**The Office for Research**

The Office for Research receives F&A recovery based only on the research grants that are submitted through University Research Centers; F&A recovery generated anywhere else is not included in OR’s calculation.

In recognition that some work of faculty who are active in the University Research Centers continues to occur in the Evanston schools and departments, the Office for Research provides funding from its shared F&A recovery income to support staff in the relevant departments.

*Source: Office for Research Planning, Finance and Communications*