OFFICE OF MANAGEMENT AND BUDGET

Cost Principles for Non-Profit Organizations; Final Revision to Provision on Interest Allowability

AGENCY: Office of Management and Budget.

ACTION: Final revision to the interest provision in OMB Circular A–122, ''Cost Principles for Non-Profit Organizations''.

SUMMARY: This notice finalizes a revision to the provision on interest allowability for non-profit organizations.

EFFECTIVE DATE: The revision is effective on September 29, 1995.

FOR FURTHER INFORMATION CONTACT: Federal agencies should contact the Office of Federal Financial Management, Office of Management and Budget, (202) 395–3993. Non-Federal organizations should contact the organization's cognizant Federal funding agency. For a copy of the Circular, contact Office of Administration, Publications Office, Room 2200, New Executive Office Building, Washington, DC 20503, or telephone (202) 395–7332.

SUPPLEMENTARY INFORMATION:

A. Background

On September 26, 1994, the Office of Management and Budget (OMB) published a proposed revision to OMB Circular A–122, ''Cost Principles for Non-Profit Organizations,'' in the Federal Register (59 FR 49090). The proposed revision was intended to encourage non-profit organizations to acquire, whether by lease or purchase, assets in the manner that would be least expensive. It provided that interest on buildings and equipment would be allowable under certain circumstances which included a favorable lease/purchase analysis, a limit on the interest rate, an offsetting of certain investment earnings against interest costs, and a needs assessment which might require pre-approval. By allowing for reimbursement of interest, OMB anticipated that many non-profit organizations would be able to enter into purchase financing arrangements which could result in long- and/or short-term savings when compared to leasing alternatives.

OMB received approximately 150 letters during the 60-day comment period from non-profit organizations, auditing firms, and government agencies. The comments were all supportive of the revision to allow interest, although some requested modifications to the criteria or clarifications regarding various aspects of the revision. As a result, as explained below, OMB has adopted the proposal with modifications.

The revision will serve to provide consistency on interest allowability across OMB's three cost principles circulars (Circular A–122; Circular A–21, ''Cost Principles for Educational Institutions;'' and Circular A–87, ''Cost Principles for State, Local and Indian Tribal Governments'') and to reduce the cost to the Federal Government of non-profit organizations' facilities.

OMB is committed to providing consistency across the three cost principles circulars with regard to cost allowability, and also to ensure that facilities cost reimbursements are reasonable and economical. Accordingly, we are hereby providing notice that efforts to establish benchmark payment rates for space used to support federally-sponsored research agreements will include both the non-profit community as well as the university community (as announced in the Federal Register (60 FR 7105) on February 6, 1995, in a proposed revision to Circular A–21). This benchmarking effort has been identified as a possible superior, long-range alternative to the needs justification being imposed by this revision to Circular A–122. If adopted, the benchmarks would eventually replace the needs justification and would form the basis for reimbursement for research space used in the conduct of federally-sponsored research.

With this final revision, Circular A–122 consists of the Circular as issued in 1980 (45 FR 46022; July 8, 1980), as amended in 1984 (49 FR 18260; April 27, 1984), in 1987 (52 FR 19788; May 27, 1987), and in this notice.

B. Comments and Responses

The comments received and OMB responses are summarized below.

Needs Assessment

Comment: The proposal would place restrictions and requirements on non-profit organizations under sponsored agreements that are not placed on commercial organizations under contracts with the Federal Government.

Response: It is true that commercial organizations with Federal contracts do not have some of the requirements, such as justifying the need for an asset, that are being applied to non-profit organizations under this revision to Circular A–122. As OMB explained in the September 1994 proposal (59 FR 49090), the Federal Government often contributes a substantial share of a non-profit organization's revenues, and this greater Federal share could decrease the incentives for non-profit organizations to make the most economical lease/purchase decisions. The requirements in the proposal were deemed to be reasonable methods of ensuring that reimbursements to non-profit organizations will be at appropriate levels. Threshold levels for these requirements were established in the final revision to reduce the paperwork burden on smaller asset purchases. Finally, it is more appropriate to compare the restrictions on non-profit organizations to those being proposed for universities under Circular A–21 (60 FR 7105), which are similar to those being instituted by this revision to Circular A–122.

Comment: Needs assessment criteria are not needed because non-profit organizations already have incentives to operate in a cost-efficient manner. To imply otherwise, mischaracterizes the funding situations faced by non-profit organizations and is factually incorrect. Also, no criteria were listed for a needs assessment. Further, the pre-approval provision will cause delays and be a resource drain on Federal agencies, short on manpower and expertise to evaluate the needs analyses, and would create confusion with the ''after-the-fact'' reviews that could result in disapproval.

Response: The ''needs assessment'' was re-termed ''needs justification,'' and is required to be prepared only for the acquisition of facilities costing over $10 million and for which the Federal Government's reimbursement is expected to equal or exceed 40 percent of the facility's cost. (The 51 percent proposed was reduced to 40 percent because of the significance of the Federal Government's investment in facilities.) The needs justification will simply provide a formal mechanism for organizations to justify their need for the facility, a significant percentage of which is being financed with Federal dollars. This justification is implicit under other provisions of Circular A–122 on excess capacity, allocability, etc. (Attachment A, A.2 and A.3; Attachment B.16). Criteria for the needs justification are specified in the revision, and OMB believes the criteria will parallel any such justification that a non-profit organization's management and board of directors would be expected to use in determining the need for additional facilities. Therefore, the needs justification would not create an administrative burden for the organization. The pre-approval aspect of the needs justification has been eliminated for many of the reasons cited

by the commentor. The requirement now calls for the preparation, rather than the submission, of the needs justification.

OMB is concerned about ensuring that costs reimbursed by the Federal Government are not excessive, as might be the case if an organization built a more expensive class A building when a less expensive class B building would suffice. Therefore, the concept of benchmark payment rates for space costs under Circulars A–122 and A–21 is being addressed by an interagency task force. Benchmarking recommendations and proposals made by this task force will be addressed in a future OMB notice to be proposed in the Federal Register. If and when the benchmark payment rates for space costs are established, OMB anticipates that the requirement for a needs justification would be eliminated.

Lease/Purchase Analysis

Comment: A lease/purchase analysis is unnecessary and potentially expensive to a non-profit organization. Lease/purchase analyses should be required only for assets costing in excess of $1 million.

Response: Lease/purchase analyses generally are performed by an organization's management as a common business practice in order to determine the costs of acquisition of expensive assets under various scenarios. Such analyses normally would be performed whether or not Federal funds are at issue, and are not expensive analysis to perform, certainly when one considers the amounts that are at stake in a real estate lease or purchase. Also, by identifying less expensive acquisition alternatives, such analyses generally pay for themselves. Circular A–122 requires that to be allowable, costs must be reasonable (Attachment A, A.3), and a lease/purchase analysis will provide such supporting documentation. However, OMB recognizes that a lease/purchase analysis may not be cost-effective for smaller facilities acquisitions. Therefore a threshold of $500,000 was established in the final revision for the lease/purchase analysis requirement for facilities. There will be no requirement for a lease/purchase analysis for equipment.

Comment: Lease/purchase analysis is arbitrary because 30–40 year leases do not generally exist for comparison to purchases.

Response: It is true that 30–40 year leases do not generally exist for comparison purposes. However, potential long term lease costs can be estimated for purposes of comparison with purchasing as an acquisition alternative. This is a common business practice for private sector companies, which must decide whether to purchase or lease the office, warehouse, or factory space they need. These estimates must be made in order to provide a comparison from which to determine the least costly alternative.

Comment: A non-profit organization should be allowed to recover interest in those circumstances when purchasing is clearly justified for management or programmatic reasons (such as when the grantee wishes to expand an existing, owned facility) or when leasing on site is not practical or is not legally permissible.

Response: OMB understands that there may be circumstances which would cause a non-profit organization to purchase an asset using debt financing even though it may be more expensive than leasing, regardless of the criteria established in this Circular. In that event, the provision at paragraph 19.a.(1)(e) does not prohibit an asset purchase, but it does limit reimbursement to the amount under the least expensive alternative, even if the organization pursues a more expensive alternative. A lease/purchase analysis is not required for renovations or alteration under Paragraph 19.a.(1)(b).

Comment: The Circular should clarify whether or not interest on land is allowable, and whether or not currently-owned land can be considered an equity contribution in a building project.

Response: It is OMB's intent that interest on land would be allowable (See Attachment B, Section 19.a.(1)). (The cost of land continues to be unallowable under Attachment B.9.c(1).) To treat interest on financing for land as an unallowable cost could otherwise skew the result of a lease/purchase analysis. Equity in currently-owned land may be considered an equity contribution to a project. Valuation of the land for purposes of determining the amount of equity shall be in accordance with OMB Circular A-110, ''Uniform Administrative Requirements for Grants and Agreements with Institutions of Higher Education, Hospitals, and Other Non-Profit Organizations,'' Subpart C, paragraph _____.23(c). For the purposes of the interest provision of Circular A–122, equity contributions may be any non-Federal contribution.

Comment: The proposal references OMB Circular A–94, ''Guidelines and Discount Rates for Benefit-Cost Analysis of Federal Programs,'' which does not apply to many non-profit organizations, and could increase costs. Also, the application of the discount rate and the present value of money calculation in the lease/purchase analysis are unnecessary and serve merely to complicate the assessment.

Response: Discount rates are commonly used in private sector lease/purchase analysis calculations of cash flows discounted for the time value of money. The provisions of Section 19.a.(1)(b) of this revision will assist in providing consistency in the calculation methodologies and discount rates used by non-profit organizations performing lease/purchase analyses. The reference to Circular A–94 has been omitted in the final revision, although the concepts of net present value found in Circular A–94 were incorporated into the final revision. Present value concepts are necessary for appropriate analysis in order to evaluate the effects of the time value of money.

Comment: The Circular should provide policy guidance to assure comparability of assumptions used in the preparation of the lease/purchase analysis.

Response: The proposal was modified to provide clarification and consistency in the preparation of the lease/purchase analysis at Paragraph 19.a.(1)(b).

Cash Flow Analysis

Comment: The ''excess cash flow'' requirements are unfair to non-profit organizations which carry all of the risk associated with purchasing a facility, while the Federal Government is at no risk. Over time, depreciation and principal payments will be equal, but a penalty on ''excess cash flow'' would result in the Federal Government's paying for less than the full cost of the use of a facility. This treatment provides incentives to lease rather than to own.

Response: The excess cash flow provisions are not related to risk of ownership, but to excessive earnings on the cash flow from allowable costs. This provision does not result in the Federal Government's paying for less than its allocable share of the allowable cost of a facility. The Federal Government will pay its allocable share of applicable interest depending upon the use of the capital asset to support Federal projects. The interest on excess cash flows simply minimizes the interest cost to the Federal Government in instances where cash flow from depreciation reimbursement exceeds debt principal payments. In order to reduce the administrative and paperwork burden on smaller acquisitions, this revision only requires interest to be calculated on excess cash flows related to debt instruments of $1 million or more, when the initial equity contribution is less than 25 percent.

Comment: The provision requires that earnings on positive cash flows be offset against interest expense. If principal payments include the cost of land, the positive cash flow and imputed earnings will be understated.

Response: The commentor is correct. Because the cost of land is unallowable (as opposed to the allowable cost of interest on land, as explained above) under Attachment B Section 9.c(1), when computing cash flows, each debt principal payment must be reduced by an amount equal to the portion of the principal payment attributable to land. The wording of the provision has been revised (Attachment B, Section 19.a.(1)(f)(ii)) to clarify how cash flow analyses are to be prepared.

Comment: The provision does not recognize the cost of the non-profit organization's capital, or equity, that is contributed to the asset acquisition, thus reducing the financing needs.

Response: In computing cash flow under Attachment B, Paragraph 19.a.(1)(f)(ii), the non-profit organization's equity contribution, regardless of the amount, is recognized and treated as an outflow along with principal and interest payments. This treatment has the effect of allowing the grantee to retain earnings on positive cash flows attributable to its equity capital. If the organization's equity contribution exceeds 25 percent, a cash flow analysis is not required and interest earnings on positive cash flow are not required to be offset against interest expense charged to Federal programs. OMB intends to study allowing the cost of an organization's own capital for consideration in future revisions to Circular A–122. OMB may also consider other alternatives to reimburse facilities costs. If and when alternative facilities reimbursement methods are developed and considered to be potentially superior to the present method, they will be published for comment in the Federal Register.

Comment: The provision will require Federal agencies to compute earnings on positive cash flows. How and at what rate is this to be performed?

Response: The provision was modified at Paragraph 19.a.(1)(f)(ii) to clarify when and how earnings are to be computed. (The three month Treasury Bill rate to be used in the calculations can be found in such publications as the *Wall Street Journal*.) OMB has developed a sample format for reporting excess cash flows, which is displayed as follows:

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A-122 Excess Cash Flow Calculation
Sample Format for Annual Report -- Applicable for debt arrangements over $1 million, unless initial equity contribution equals 25% or more

Year ____ of ____ Years		Month 1	2	3	4	.....	12	Annual Total
Line 1	Prior period's cumulative cash flow balance (Prior Month's or Year's Line 9)							
	Add this period's inflows:							
Line 2	Depreciation expense (Note 1)							
Line 3	Interest expense (Note 2)							
Line 4	Amortization of debt issuance costs (Note 2)							
	Subtract this period's outflows:							
Line 5	Principal payments (Note 3)							
Line 6	Interest payments (Note 3)							
Line 7	Subtotal of cumulative cash flows (Line 1+2+3+4-5-6)							
Line 8	In initial period only, subtract initial equity contribution(Note 4) (Will be zero after initial period)							
Line 9	Total of cumulative cash flows (In initial period, Line 7 - Line 8) (In subsequent periods, equals Line 7)							
Line 10	If line 9 is positive, state month's closing interest rate on 3-month Treasury Bill If line 9 is negative, put "0" (zero)							
Line 11	Imputed interest income on cumulative positive cash flow Monthly columns = (Line 10 x Line 9)/12							
Line 12	Allowable interest for period (Line 6 - Line 11)							

Note 1: May include amortization of capitalized construction interest in accordance with GAAP. Depreciation expenses should be reported on a monthly basis (Annual expense/12).

Note 2: Interest expense and amortization of debt issuance costs that are not included in loan amount should be reported on a monthly basis (Annual expense/12).

Note 3: If land is included in the financing arrangement, Line 5 would be calculated as: principal payment - (Debt proceeds used to purchase land / total debt proceeds x principal payment). Principal and interest payments should be reported in the month that payments were made.

Note 4: This line may only include amounts of initial equity contribution made prior to occupancy of the facility. The amount is to be entered only in the initial period covered by the cash flow submission, and should be left blank in future periods.

Other

Comment: Definitions for a number of terms should be included, e.g., equity contribution, re-acquired assets, and asset cost.

Response: Definitions of terms have been added to the final revision in Attachment B, Paragraph 19.a.(3).

Comment: The provision should provide a disclaimer of the Federal Government's liability regarding the debt incurred by a non-profit organization when financing assets to be used in the fulfillment of sponsored agreements.

Response: OMB does not express or imply any long-term obligation on the part of the Federal Government to continue or increase funding for sponsored agreements covered by this Circular. Nor does it express or imply any obligation or liability to a non-profit organization or any third party with respect to any financial borrowing or other financing arrangement entered into by a non-profit organization to purchase an asset.

Comment: Excess capacity costs should be unallowable, with a one year grace period.

Response: The costs of initial excess capacity are unallowable under the allocability and allowability provisions of this Circular found at Attachment A, Paragraph 2.a and Attachment B, Paragraph 16 which do not allow exceptions for excess capacity in newly-acquired space.

Comment: Interest costs of fully depreciated assets should also be unallowable.

Response: Under the allocability provision found at Attachment A, Paragraph 2.a, the interest costs on fully-depreciated, retired, scrapped, or non-existent assets are unallowable.

Comment: In the best interests of the Federal Government, the provision should allow for the prior existence of special agreements which already allowed interest.

Response: OMB does not intend for the revision to replace any written agreements between non-profit organizations and the Federal Government that were made prior to the effective date of this revision.

Comment: Professional fees associated with the purchase of real property should be allowable.

Response: Usual and customary professional fees and related costs and fees associated with, and necessary to, the acquisition of real property are allowable under Attachment B, Paragraph 9 whether expensed or capitalized, in accordance with Generally Accepted Accounting Principles (GAAP).

Comment: Many non-profit organizations are being forced to decide on debt-financed property purchases before the change to Circular A–122 is adopted. The rule should have a retroactive date and/or allow interest incurred after the effective date, regardless of the asset acquisition date if the criteria set forth are met.

Response: If interest were to be allowed on assets purchased before the effective date of this revision, the Federal Government would incur the substantial cost on debt arrangements entered into by non-profit organizations with full knowledge that interest was an unallowable cost. In addition, these prior purchases were obviously not made in accordance with the requirements that are being announced here. Also, changes to interest allowability under Circulars A–21 and A–87 have, similarly, not been applied retroactively.

Comment: The substantial relocation provision raises more issues than it solves and is inconsistent with Executive Order 12866 calling for streamlined regulations. Also, it suggests that the Federal Government is in a better position than the non-profit organization to make relocation decisions. If retained, the substantial relocation provision should be limited to 20 years.

Response: The substantial relocation provision at Attachment B, Paragraph 19.a.(1)(f)(iii) exists to ensure that the location of Federal program operations is not shifted unnecessarily, or ''churned,'' to other debt-financed facilities after a debt instrument is substantially retired. By churning Federal programs into debt-financed buildings, the Federal Government carries the burden of costs of facilities expansion that should reasonably be shared with non-Federal entities. If such a relocation is needed, the cognizant Federal agency must be notified and an adjustment of the indirect cost rate may be necessary. The relocation does not require approval of the Federal cognizant agency, as was originally proposed. (However, if interest will be claimed on the new location, then the provisions of Paragraph 19.a. apply.) A time limit of 20 years was added to this provision.

Comment: The provision should cover financing of alterations and renovations.

Response: The provision was modified at Attachment B, Paragraph 19.a.(1) to clarify the allowability of interest on financing of alterations and renovations. Alterations and renovations will not require a needs justification.

Comment: The provision should clarify whether ''re-acquired assets'' include replacement assets.

Response: The provision was modified at Paragraph 19.a.(1) to clarify the allowability of interest on replacement assets. However, interest will not be allowable for re-acquired assets (Paragraph 19.a.(1)(f)(i)).

Comment: ''Fair market interest rate'' should be qualified to similarly-situated organizations borrowing from a third party.

Response: The provision was modified at Paragraph 19.a.(1)(b) to limit reimbursement to the fair market borrowing rates available to the organization from an unrelated (''arm's length'') third party. This provision is intended to prevent the Federal Government from reimbursing organizations for interest at higher rates than necessary.

Comment: The provision should address situations of leasing and buying to/from related parties.

Response: The revision eliminates the profit in related party transactions by limiting interest expense reimbursement to a rate no higher than available from an unrelated third party (Attachment B, Paragraph 19.a.(1)(c)) and by limiting allowable costs related to the purchase price of assets to the fair market value available from an unrelated third party (Attachment B, Paragraph 19.a.(1)(f)(iv)). Also, Attachment B, Paragraph 42.c. of the Circular provides that ''Rental cost under less-than-arms-length leases are allowable only up to the amount that would be allowed had title to the property vested in the organization.''

Comment: The provision should state that interest on capital leases is allowable.

Response: The provision was modified at Attachment B, Paragraph 19.a.(1) to clarify the allowability of interest under capital leases, but a revised Attachment B, Paragraph 42.d. limits reimbursement to the allowable costs of ownership, such as depreciation, maintenance, taxes, and insurance. Unallowable costs include amounts paid for profit, management fees, and taxes that would not have been incurred had the organization purchased the facility. To satisfy the lease/purchase analysis requirement, an analysis could be prepared to compare either the costs of an operating lease versus a capital lease, or a capital lease versus a purchase.

Comment: The provision should clarify that adjustable rate financing methods are acceptable.

Response: OMB does not prescribe the form that borrowing arrangements must take in order to be allowable. Therefore,

the provision allows interest regardless of whether interest rates are fixed or variable, but assumes that the rates are market rates.

Comment: The proposed wording results in an unintended effective restriction upon debt structures with variable or deferred repayment terms, such as balloon loans.

Response: The provision is not intended to restrict the structuring of debt repayment arrangements. However, it is designed to minimize cost to the Federal Government where principal payments are delayed, thus increasing interest costs. Under a balloon payment arrangement, interest is charged on the full amount of the principal for the full term of the loan. In order to reduce the interest costs that the Federal grants will be charged, the revision has the effect of encouraging debt structures where the principal is paid down on a regular basis.

Comment: The Circular does not specify whether predetermined multiple-year indirect cost rates can be established for non-profit organizations that incur interest costs for capital assets since the Federal participation of space in the new facility may vary from year to year.

Response: Predetermined multiple-year indirect cost rates can be established for non-profit organizations if the Federal cost negotiators can determine the reasonableness and acceptability of space projections provided by the non-profit organizations, regardless of whether interest costs are incurred in financing the asset.

Alice M. Rivlin,

Director.

Revisions to Attachment B of Circular A–122

The following paragraphs replace paragraph 19.a of Attachment B to Circular A–122:

19. Interest, fundraising, and investment management costs.

a. Interest.

(1) Costs incurred for interest on borrowed capital or temporary use of endowment funds, however represented, are unallowable. However, interest on debt incurred after the effective date of this revision to acquire or replace capital assets (including renovations, alterations, equipment, land, and capital assets acquired through capital leases), acquired after the effective date of this revision and used in support of sponsored agreements is allowable provided that:

(a) For facilities acquisitions (excluding renovations and alterations) costing over $10 million where the Federal Government's reimbursement is expected to equal or exceed 40 percent of an asset's cost, the non-profit organization prepares, prior to the acquisition or replacement of the capital asset(s), a justification that demonstrates the need for the facility in the conduct of federally-sponsored activities. Upon request, the needs justification must be provided to the Federal agency with cost cognizance authority as a prerequisite to the continued allowability of interest on debt and depreciation related to the facility.

The needs justification for the acquisition of a facility should include, at a minimum, the following:

- A statement of purpose and justification for facility acquisition or replacement
- A statement as to why current facilities are not adequate
- A statement of planned future use of the facility
- A description of the financing agreement to be arranged for the facility
- A summary of the building contract with estimated cost information and statement of source and use of funds
- A schedule of planned occupancy dates

(b) For facilities costing over $500,000, the non-profit organization prepares, prior to the acquisition or replacement of the facility, a lease/purchase analysis in accordance with the provisions of OMB Circular A–110, ''Uniform Administrative Requirements for Grants and Agreements with Institutions of Higher Education, Hospitals and Other Non-Profit Organizations,'' sections _____.31 through _____.37, which shows that a financed purchase or capital lease is less costly to the organization than other leasing alternatives, on a net present value basis. Discount rates used should be equal to the non-profit organization's anticipated interest rates and should be no higher than the fair market rate available to the non-profit organization from an unrelated (''arm's length'') third-party. The lease/purchase analysis shall include a comparison of the net present value of the projected total cost comparisons of both alternatives over the period the asset is expected to be used by the non-profit organization. The cost comparisons associated with purchasing the facility shall include the estimated purchase price, anticipated operating and maintenance costs (including property taxes, if applicable) not included in the debt financing, less any estimated asset salvage value at the end of the period defined above. The cost comparison for a capital lease shall include the estimated total lease payments, any estimated bargain purchase option, operating and maintenance costs, and taxes not included in the capital leasing arrangement, less any estimated credits due under the lease at the end of the period defined above. Projected operating lease costs shall be based on the anticipated cost of leasing comparable facilities at fair market rates under rental agreements that would be renewed or reestablished over the period defined above, and any expected maintenance costs and allowable property taxes to be borne by the non-profit organization directly or as part of the lease arrangement.

(c) The actual interest cost claimed is predicated upon interest rates that are no higher than the fair market rate available to the non-profit organization from an unrelated (''arm's length'') third party.

(d) Investment earnings, including interest income, on bond or loan principal, pending payment of the construction or acquisition costs, are used to offset allowable interest cost. Arbitrage earnings reportable to the Internal Revenue Service are not required to be offset against allowable interest costs.

(e) Reimbursements are limited to the least costly alternative based on the total cost analysis required under (b). For example, if an operating lease is determined to be less costly than purchasing through debt financing, then reimbursement is limited to the amount determined if leasing had been used. In all cases where a lease/purchase analysis is performed, Federal reimbursement shall be based upon the least expensive alternative.

(f) Non-profit organizations are also subject to the following conditions:

(i) Interest on debt incurred to finance or refinance assets acquired before or reacquired after the effective date of this Circular is not allowable.

(ii) For debt arrangements over $1 million, unless the non-profit organization makes an initial equity contribution to the asset purchase of 25 percent or more, non-profit organizations shall reduce claims for interest expense by an amount equal to imputed interest earnings on excess cash flow, which is to be calculated as follows. Annually, non-profit organizations shall prepare a cumulative (from the inception of the project) report of monthly cash flows that includes inflows and outflows, regardless of the funding source. Inflows consist of depreciation expense, amortization of capitalized construction interest, and annual interest expense. For cash flow calculations, the annual inflow figures shall be divided by the number of

months in the year (usually 12) that the building is in service for monthly amounts. Outflows consist of initial equity contributions, debt principal payments (less the pro rata share attributable to the unallowable costs of land) and interest payments. Where cumulative inflows exceed cumulative outflows, interest shall be calculated on the excess inflows for that period and be treated as a reduction to allowable interest expense. The rate of interest to be used to compute earnings on excess cash flows shall be the three month Treasury Bill closing rate as of the last business day of that month.

(iii) Substantial relocation of federally-sponsored activities from a facility financed by indebtedness, the cost of which was funded in whole or part through Federal reimbursements, to another facility prior to the expiration of a period of 20 years requires notice to the Federal cognizant agency. The extent of the relocation, the amount of the Federal participation in the financing, and the depreciation and interest charged to date may require negotiation and/or downward adjustments of replacement space charged to Federal programs in the future.

(iv) The allowable costs to acquire facilities and equipment are limited to a fair market value available to the non-profit organization from an unrelated (''arm's length'') third party.

(2) For non-profit organizations subject to ''full coverage'' under the Cost Accounting Standards (CAS) as defined at 48 CFR 9903.201, the interest allowability provisions of paragraph 19.a. do not apply. Instead, these organizations' sponsored agreements are subject to CAS 414 (48 CFR 9903.414), cost of money as an element of the cost of facilities capital, and CAS 417 (48 CFR 9903.417), cost of money as an element of the cost of capital assets under construction.

(3) The following definitions are to be used for purposes of paragraph 19:

(a) ''Re-acquired assets'' means assets held by the non-profit organization prior to the effective date of this revision that have again come to be held by the organization, whether through repurchase or refinancing. It does not include assets acquired to replace older assets.

(b) ''Initial equity contribution'' means the amount or value of contributions made by non-Federal entities for the acquisition of the asset or prior to occupancy of facilities.

(c) ''Asset costs'' means the capitalizable costs of an asset, including construction costs, acquisition costs, and other such costs capitalized in accordance with General Accepted Accounting Principles (GAAP).

The following paragraph replaces paragraph 42.d. of Attachment B to Circular A–122):

42. Rental Costs.

d. Rental costs under leases which are required to be treated as capital leases under Generally Accepted Accounting Principles (GAAP), are allowable only up to the amount that would be allowed had the organization purchased the property on the date the lease agreement was executed, i.e., to the amount that minimally would pay for depreciation or use allowances, maintenance, taxes, and insurance. Interest costs related to capitalized leases are allowable to the extent they meet criteria in Attachment B, paragraph 19.a. Unallowable costs include amounts paid for profit, management fees, and taxes that would not have been incurred had the organization purchased the facility.

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OFFICE OF MANAGEMENT AND BUDGET

Cost Principles for Non-Profit Organizations; Proposed Revisions

AGENCY: Office of Management and Budget.

ACTION: Proposed revisions to OMB Circular A–122, ''Cost Principles for Non-Profit Organizations''.

SUMMARY: This notice proposes changes to OMB Circular A–122, ''Cost Principles for Non-Profit Organizations,'' to revise the definition of equipment, to make certain additional costs unallowable, to modify the multiple allocation base method for computing indirect cost rate(s), and to place a ceiling on the administrative portion of indirect costs for organizations with Federal funding over $10 million. The proposed changes provide consistency across OMB's cost principles Circulars A–122; A–87, ''Cost Principles for State and Local Governments;'' and A–21, ''Cost Principles for Educational Institutions.''

DATES: Comments on these proposals are due December 5, 1995.

ADDRESSES: Comments should be mailed to Financial Standards and Reporting Branch, Office of Federal Financial Management, Office of Management and Budget, 725 17th Street, N.W., Room 6025, Washington, DC 20503. Comments up to three pages in length may be submitted via facsimile to 202–395–3952. Electronic mail comments may be submitted via Internet to TRAN__H@A1.EOP.GOV. Please include the full body of electronic mail comments in the text and not as an attachment. Please include the name, title, organization, postal address, and E-mail address in the text of the message.

FOR FURTHER INFORMATION CONTACT: Non-Federal organizations should contact the organization's cognizant Federal agency. Federal agencies should contact Gilbert Tran, Financial Standards and Reporting Branch, Office of Federal Financial Management, Office of Management and Budget, (202) 395–3993.

SUPPLEMENTARY INFORMATION: In this issue of the Federal Register, the Office of Management and Budget (OMB) issued a final revision to OMB Circular A–122, ''Cost Principles for Non-Profit Organizations,'' regarding interest allowability. The revision was made in a continuing effort to provide consistency across OMB's cost principles Circulars A–122; A–87, ''Cost Principles for State and Local Governments;'' and A–21, ''Cost Principles for Educational Institutions,'' to ensure more comparable treatment of various types of institutions when seeking support from the Federal Government, and to promote cost effective funding decisions on the part of the Federal Government and non-profit organizations. Circular A–122 consists of the Circular as originally issued in 1980 (45 FR 46022; July 8, 1980), with amendments in 1984 (49 FR 18260; April 27, 1984), in 1987 (52 FR 19788; May 27, 1987) and in this issue. See also 60 FR 36316 (July 14, 1995) regarding equipment capitalization threshold waivers.

To further the goals stated previously, OMB proposes herein to revise the definition for equipment, to make certain additional types of costs unallowable, to modify the multiple allocation base method for computing indirect cost rate(s), and to place an upper-limit on payments for administrative expenses. The following describes each of the four proposals.

First, in the equipment definition in Attachment B, section 15, OMB is proposing to raise the threshold amount to $5000 in conformance with the threshold established in Circular A–110, ''Uniform Administrative Requirements for Grants and Agreements with Institutions of Higher Education, Hospitals, and Other Non-Profit Organizations'' (58 FR 62992; November 29, 1993). This revision will decrease burdens associated with accounting for property.