Department of Health and Human Services

DEPARTMENTAL APPEALS BOARD

Appellate Division

SUBJECT: Benaroya Research Institute DATE: September 12, 2008
Docket No. A-08-82
Decision No. 2197

DECISION

Benaroya Research Institute (BRI), a nonprofit organization located in Seattle, Washington, appeals a determination by the Division of Cost Allocation (DCA) not to allow depreciation on improvements to the fourth floor of BRI's building. The improvements were made by BRI's former tenant and used in BRI's federally-funded research after the tenant left the premises. BRI proposed to include $131,875 for annual depreciation on the improvements in a cost pool used to determine the indirect cost rate that applies to BRI's federal grants and contracts for medical research for the year 2006. DCA determined that BRI had incurred no acquisition cost for the improvements and that BRI's independent auditors did not recognize the depreciation on BRI's financial statements. Thus, DCA determined it could not allow the proposed depreciation in the indirect cost pool in 2006 or in future years.

For the reasons explained below, we sustain DCA's determination and reject BRI's alternative proposals for including in the indirect cost pool an amount for either depreciation or a use allowance for the tenant improvements. Based on the record before us, we conclude that BRI has not established what, if any, acquisition cost it incurred for the improvements – a prerequisite for determining the allowable amount for either depreciation or a use allowance - and has not shown that allowing any depreciation or a use allowance under the circumstances here would be consistent with generally accepted accounting principles and BRI's financial statements, as required.

Legal Background

Office of Management and Budget Circular A-122 (OMB A-122) provides a uniform set of cost principles for determining the

allowability of costs charged to federal grants, contracts, and other agreements; it is designed to promote efficiency and understanding between nonprofit grantees and the federal government. OMB A-122 is codified at 2 C.F.R. Part 230 and made applicable to HHS grants to nonprofit organizations by 45 C.F.R. § 74.27(a). It provides that the total cost of an award is the sum of the allowable direct and allocable indirect costs less any applicable credits. Among other requirements, costs charged to federal awards must be allocable thereto, allowable types of costs, adequately documented, and determined in accordance with generally accepted accounting principles (GAAP). 2 C.F.R. Part 230, Appendix (App.) A, ¶ A.

Compensation for a grantee's use of buildings, other capital improvements, and equipment "may be made through use allowance or depreciation." Id. at App. B, ¶ 11.a. Grantees may claim depreciation or use allowances as "[i]ndirect costs . . . that have been incurred for common or joint objectives and cannot be readily identified with a particular final cost objective." Id. and App. A, ¶ C.1, C.2. The computation of use allowances or depreciation "shall be based on the acquisition cost of the assets involved. The acquisition cost of an asset donated to the non-profit organization by a third party shall be its fair market value at the time of the donation." App. B, ¶ 11.b. Use allowances are computed at an annual rate not exceeding two percent of acquisition cost for "buildings and improvement," and six and two-thirds percent of acquisition cost for equipment, including equipment which is merely attached or fastened to the building but not permanently fixed to it, such as "counters" and "laboratory benches bolted to the floor;" equipment will be considered as not being permanently fixed to the building if it can be removed without the need for costly or extensive alterations or repairs to the building or the equipment. Id. at ¶ 11.g.

Indirect costs are normally distributed and charged to federal awards by the use of an indirect cost rate. App. A, ¶ D.2; Texas Health and Human Services Commission, DAB No. 2136, at 5 (2007); Council for Economic Opportunities in Greater Cleveland, DAB No. 1980, at 2 (2005), Graduate Hospital, DAB No. 1723, at 4 (2000). An "indirect cost rate" is a method of distributing joint costs to benefitting cost objectives. Basically, a rate is determined by dividing total indirect costs by a direct cost distribution base, either total salaries and wages or "modified total direct costs" (that is total direct costs minus costs that might distort the distribution). The resulting rate (expressed as a percentage) is then applied to equivalent direct costs of the particular grant program or project to determine the amount of

indirect costs allocable to that program or project. For large grantees, calculation of an indirect cost rate can be very complicated, with various rates calculated for different cost pools. A grantee seeking to claim indirect costs under federal awards develops its indirect cost rate through negotiation with the cognizant federal agency, in this case HHS, through DCA, following submission of an indirect cost rate proposal. Part 230, App. A, ¶ E. Each indirect cost rate proposal must be accompanied by, and be cross referenced and reconciled to, the grantee's independently audited financial statements which account for all activities during the fiscal year on which the proposal is based. OASMB-5, *Cost Principles and Procedures for Establishing Indirect Cost and Other Rates for Grants and Contracts with HHS, A Guide for Nonprofit Organizations*, at 3 (DCA Ex. 1, at 8).

The Board has repeatedly held that a grantee bears the burden of documenting the existence and allowability of its costs. Central Piedmont Action Council, Inc., DAB No. 1916, at 10 (2004); Kuiqpaqmiut, Inc., DAB No. 1780, at 3 (2001); Ohio Valley Opportunities, Inc., DAB No. 1390, at 2 (1993), and cases cited therein; see also Northstar Youth Services, Inc., DAB No. 1884, at 5 (2003) (once a cost is questioned as lacking documentation, the grantee bears the burden to document that the costs were actually incurred and represent allowable costs that are allocable to the grant).

Factual Background

The following facts appear from the record and are undisputed, except as indicated. BRI received approximately $2.26 million in federal grants and contracts for medical research during 2006, principally through programs administered by the National Institutes of Health. DCA Ex. 4, at 7; BRI Exs. B; K, at K-1. In October 1999, BRI leased the fourth floor of its building in Seattle to Amgen (at that time called Immunex) Corp. for use as a biomedical research facility, for a term of ten years beginning in 2000 with an option for Amgen to extend the lease for an additional three years. BRI Ex. E (lease agreement). The lease required Amgen to improve the building's fourth floor, which was unimproved shell space, by installing "wet lab bench space in at least seventy-five percent (75%) of the net rentable square footage in the Premises." BRI Ex. E, at E-6; BRI Reply Brief (Br.) at 3. The improvements were "and remain the property of [BRI]." Id. The parties report the cost of the improvements as

$3,575,895.59 (BRI) or $3,336,000 (DCA).[1] Under the agreement, if BRI terminated Amgen's option to extend the lease for an additional three years, or terminated the lease in response to Amgen's attempt to assign the premises to an unapproved party, BRI was to pay Amgen for the remaining, unamortized value of the improvements. BRI Ex. E, at E-20, E-37, E-38.

Amgen terminated the lease effective June 20, 2005 because, according to BRI, Amgen was consolidating "a large number of its local acquisitions/groups" in "an enormous local facility" it had constructed. BRI Exs. H; J, at J-7. By agreement with BRI, Amgen paid BRI $727,366 as "sole and exclusive compensation for the early termination of the lease." BRI Ex. H. This agreement does not mention the tenant improvements or their unamortized value.

BRI occupied the fourth floor and used the improvements in its federally-funded medical research as of June 2005. BRI Ex. K, at K-3. BRI sought to include $131,875 in annual depreciation for the fourth floor tenant improvements in its indirect cost pool for 2006 (and presumably for future years), used to determine its indirect cost rate for on-site research. BRI Reply Br. at 4; DCA Ex. 2. BRI calculated that amount by depreciating the appraised value of the improvements, $3,165,000 as of June 2005, over their projected remaining useful life of 24 years, using a straight-line depreciation method. BRI Ex. I (appraisal); DCA Ex. 2. DCA rejected BRI's proposal, and approved a final rate for on-site research for 2006 of 81.3% of modified total direct costs and a provisional rate for on-site research for 2007 and 2008 of 83% of modified total direct costs. BRI Ex. D, at D-4. DCA calculated these rates after removing the proposed depreciation cost from the indirect cost pool.

Analysis

I. BRI has not established what, if any, acquisition cost it incurred for the tenant improvements.

The computation of use allowances or depreciation is based on the "acquisition cost" of the assets involved. 2 C.F.R. Part 230, App. B, ¶ 11.b. Although BRI's tenant, Amgen, paid for the improvements as a requirement of the lease, BRI argues that it incurred the acquisition cost in the form of foregone rental

[1] BRI cites 2001 correspondence from Immunex enclosing invoices; DCA cites a 2008 e-mail from BRI stating the cost to complete the construction. BRI Br. at 3, citing BRI Ex. G; DCA Ex. 2.

income, in that it could have charged Amgen higher rent for the fourth floor space if BRI had installed and paid for the improvements itself. BRI argues that its claim for depreciation or a use allowance would have been allowed had BRI paid for the improvements directly and charged Amgen higher rent, rather than requiring Amgen to assume responsibility for the improvements. BRI asserts that "[g]iven that the value of the leasehold improvements was $3,575,986 at the time of completion of the tenant improvements, the 'foregone rental income' was equal to this amount." BRI Br. at 13.

BRI's argument, while initially appealing, does not withstand scrutiny. As DCA points out, the hypothetical transaction BRI describes is not what occurred here. Instead, BRI entered into a lease under which Amgen bore the cost of the improvements and they were treated as tenant improvements, despite the fact that BRI was considered the owner. The GAAP provisions that BRI cites indicate that tenant-funded improvements are to be capitalized by <u>the tenant</u> and amortized over the lease term. BRI Br. at 7-8, citing BRI Ex. L. BRI admitted that Amgen used some of the asset value of the improvements prior to the early termination of the lease.[2] BRI Br. at 13. Contrary to what BRI argues in its reply brief, the lease terms do not support a finding that Amgen in fact paid a reduced rent amount because it was paying for the improvements. BRI Reply Br. at 5-6. For example, the lease provided that the tenant was to pay rent "without deduction or offset (except as otherwise set forth in this Lease) . . . ." BRI Ex. E, at E-6. The only rent credit provided for in the lease was for "demising work" pursuant to Exhibit L of the lease at a cost of roughly $60,000, and this work was separate from the tenant improvements at issue here, which were done pursuant to Exhibit C to the lease. <u>Id.</u> at E-39, ¶ 37; E-45 – E-57 (Lease Ex. C); E-60 – E-66 (Lease Ex. L). BRI has submitted no evidence that, in determining the amount of the rent as set out in the lease agreement, the parties took the tenant improvements into account. Thus, BRI has not met its burden of establishing that it incurred a cost in the form of foregone rental income to acquire the improvements.

Even accepting BRI's theory that it paid for the improvements through foregone rent, BRI has not met its burden to document the amount of any such cost. BRI argues that its acquisition cost was equal to Amgen's cost for the improvements in 1999-2000, but

[2] A finding that Amgen depreciated or amortized the cost of the improvements is also supported by BRI's argument that DCA should permit BRI to claim depreciation associated with the "unamortized value" of the improvements. BRI Br. at 15.

what Amgen acquired was different from what BRI expected to acquire under the lease. Under the original lease, Amgen had the right to use the improvements for at least ten years, with an option for three more years, as well as the right to amortize the cost of the improvements over the lease term, a shorter period of time than their useful life of 30 years, and a right to payment for any unamortized value if BRI took possession before the 13 years expired. Thus, it is neither logical nor credible to think that BRI would have reduced the rent to reflect the <u>entire</u> cost to Amgen for making the improvements. Certainly, any rent reduction would have been offset by the value of the benefits to Amgen from constructing the improvements. Moreover, any rent reduction logically would also have taken into account the fact that BRI had an expectation of having use of the improvements after 13 years (or sooner if Amgen did not exercise the option to extend the lease), as well as the benefit to BRI from having Amgen pay for the improvements and agree to assume responsibility for managing construction of the improvements. BRI Ex. E, at E-45 - E-52.

BRI seeks alternatively to treat the $3,165,000 appraised value of the improvements as of June 30, 2005 as the value of "the remaining 'foregone rental income.'" BRI Br. at 13, Br. Ex. I. The appraisal, however, was not done until 2005 and therefore could not have been the basis for determining how much rent BRI would forego (if, indeed, it did forego any rent). Moreover, if the $3,165,000 represents the "remaining" foregone rental income, this would suggest that the rental income that was "foregone" by BRI during Amgen's tenancy was merely the roughly $410,000 difference between the acquisition cost to Amgen and the remaining value. Yet, BRI's indirect cost rate proposal treated the $3,165,000 as its acquisition cost, not the $410,000. We also note that, although the appraisal says that depreciation of the improvements was taken into account, the appraisal does not indicate that what it took into account was the amount of the depreciation/amortization taken by Amgen. The appraisal does not identify the amount of depreciation/amortization taken by Amgen during the period of its tenancy. BRI Ex. I. Using the "appraised value" as of June 30, 2005, thus fails to recognize the extent to which the improvements were previously depreciated or amortized by Amgen. BRI provided no information from which we can determine the remaining unamortized value of the improvements, which would be relevant in evaluating BRI's potential cost under the lease to acquire early use of the assets.[3]

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[3] This failure to provide any information about the extent (continued...)

BRI provided no other evidence that establishes the existence or amount of the cost it claims to have incurred through foregone rent. BRI did not provide, for example, expert testimony or other evidence establishing applicable rental rates for improved versus unimproved space. While BRI submitted a slide from a presentation it gave to DCA asserting that its third floor space leased for approximately $20.00 more per square foot per month than the fourth floor space, it did not rely on this exhibit in its briefs. BRI Ex. J, at J-9. We do not, in any event, consider the presentation reliable to establish either that any difference in rent amounts was because of the fourth floor improvements or that the total rent reduction was $357,000 per year, as the presentation suggests. Id. The figures in the presentation are not reliable, for the following reasons: (1) the rent figure BRI gave for the fourth floor is only the "basic rent" amount, but the lease provided for "additional rent" equal to BRI's actual expenses allocable to the premises; (2) BRI provided no information to show that any improvements to the third floor space were comparable to the tenant improvements at issue here; and (3) in calculating the total alleged lost rent, BRI's presentation multiplied the rent difference per square foot by 17,837 square feet, but the appraisal report indicates that the improved space on the fourth floor was approximately 15,520 square feet. Id.; BRI Ex. E, at E-5, E-13 - E-18; BRI Ex. I, at I-6.

Finally, it is significant that BRI did not show that, when the lease was terminated early by Amgen, BRI paid Amgen for the remaining, unamortized value of the improvements, as the lease would have required had BRI precipitated an early termination. BRI Ex. E, at E-38. Instead, Amgen paid BRI $727,366.[4] BRI Ex.

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[3](...continued) to which the improvements were previously amortized by Amgen is significant in light of BRI's citation of a provision from Part 230 permitting negotiation of depreciation or a use allowance for the unamortized portion of equipment written off as a result of a change in capitalization levels. BRI has not established the unamortized amount of the costs of the improvements nor shown how that amount can be determined absent information about how Amgen treated the improvements. In any event, as we discuss elsewhere in this decision, this provision is not applicable to the claimed costs.

[4] There is no support for BRI's assertion that Amgen made this payment in part to be "released from . . . its obligation to repair, decontaminate, thoroughly wash, and obtain an environmental inspection of the lease space upon surrender of the

(continued...)

H. The lease's requirement that BRI compensate Amgen for the remaining value of improvements if BRI terminated the lease early indicates that Amgen, not BRI, incurred the cost of the improvements. The facts further suggest the possibility that there was no unamortized value remaining for the improvements. Absent any evidence that any of the cost remained unamortized upon early termination of the lease or other evidence that the improvements were a factor in the parties' negotiations over the termination, we are unwilling to infer that they were. BRI takes issue with DCA's characterization of the $727,366 payment from Amgen as a "windfall." DCA Br. at 9. But, this is not an unfair characterization under the circumstances. BRI itself occupied and had a need for the space at the time of the termination, and, even if BRI had not had a need for the space, Amgen had taken steps to locate a new tenant and therefore to mitigate any potential loss of rent from early termination of the lease. BRI Ex. H. More important, to the extent BRI suggests there was a cost to it for the tenant improvements because BRI would have received a higher payment from Amgen but for the tenant improvements, BRI has not shown that the tenant improvements were a factor in the negotiations, much less the extent to which Amgen's payment to it would have been higher but for the tenant improvements. The document providing for the payment to BRI says the agreement to change the lease expiration date is "[i]n exchange for the consideration set forth herein," but nothing in the document identifies the tenant improvements as part of the consideration. Id.

Thus, BRI has not shown what, if any, cost it incurred to acquire the improvements.

DCA's denial of BRI's request for depreciation or a use allowance is, therefore, consistent with the cost principles' goal that the federal government "bear its fair share" of costs. 2 C.F.R. § 230.15. BRI complains that the federal government has obtained use of the improvements "for free." BRI Reply Br. at 8. However, BRI has not shown what, if any, cost it incurred to obtain the improvements, and therefore has not shown what the government's "fair share," if any, should be. Indeed, allowing federal reimbursement for depreciation or a use allowance in the

[4](...continued)
premises," as required by section 5.2.11 of the lease. BRI Reply Br. at 3; see BRI Ex. E, at E-13, E-22. Instead, BRI acknowledged in the termination agreement "that . . . [Amgen] has decommissioned the [p]remises in accordance with" section 5.2.11 and had completed its obligations to clean, repair and restore the premises. BRI Ex. H, at H-1.

absence of any acquisition cost to the grantee could result in the grantee realizing a profit from its grant awards, where no provision for profit is intended. See, e.g., 45 C.F.R. § 74.81.

II. Provisions in Part 230 on depreciation of donated assets do not apply.

BRI argues that the definition in Part 230 of "acquisition cost" with respect to assets donated to a nonprofit organization by a third party - the fair market value at the time of the donation - indicates that the grantee need not directly incur the acquisition cost to receive depreciation or a use allowance. App. B, ¶ 11.b. BRI argues that the tenant improvements here should be treated like donated assets and therefore had a definite acquisition cost comparable to the fair market value.

To the extent that the cost principles recognize fair market value as the "acquisition cost" of donated assets, that provision does not apply here, as Amgen did not donate the tenant improvements to BRI. BRI's initial acquisition of title to the improvements and subsequent acquisition of the right to use the improvements resulted from commercial transactions between BRI and Amgen involving the exchange of value and contractual commitments. That Amgen agreed to pay for the improvements in expectation of enjoying their exclusive use for at least the term of the lease and later paid BRI to be released early from its obligations under the lease establishes that the improvements were not "donated" in any common sense of the word. Moreover, BRI concedes that its independent auditors determined that the improvements could not be reflected on BRI's financial statements as donated assets. BRI Br. at 9.

DCA's finding that there was no donation is not inconsistent with DCA's determination that BRI had no acquisition cost in the improvements, as BRI suggests. BRI Reply Br. at 2, 6-7. The treatment of fair market value as the acquisition cost of donated assets is expressly addressed in the cost principles because otherwise it would not be clear that a grantee would have any "acquisition cost" in a donated asset for purposes of depreciation or a use allowance. With respect to assets that are not donated, however, the plain meaning of "acquisition cost" applies. While BRI might be correct that a "cost" could be incurred by a grantee to acquire an asset even if it did not pay out funds to another entity, the grantee would still need to establish, among other things, that it did in fact incur a cost to acquire the asset in question and what the amount of that cost was. BRI did not do that here.

BRI argues that Eunice Kennedy Shriver Center for Mental Retardation, Inc., DAB No. 18 (1976), permitted a use allowance for property costs incurred by a third party and thus supports a use allowance with respect to the costs Amgen incurred. That holding, which the Board stated was based on a "unique set of facts not likely to be repeated" and "therefore not intended to set any general precedent," does not support BRI's claim. Id. at 1. The property in that case was a State-owned building that the State committed to the grantee's exclusive use in the grant project for at least 20 years. The State had promised the federal agency that the building would be used for grant purposes, the grantee appeared to be the only entity suitable to fulfil that commitment, and it was "questionable" whether the State would retain a complete title to the building if the grantee was unable to carry out the project and no replacement could be found. Id. at 3. The Board concluded that the grantee "constructively owned" the building for the purpose of cost principles then in effect authorizing use allowances when depreciation or other equivalent costs are not considered. Id. at 1, 3, 5. In so doing, the Board, as BRI notes, found no requirement in those cost principles that the grantee hold legal title to the building, which was the agency's objection to permitting a use allowance. Here, for assets that have not been donated to the grantee, the cost principles limit reimbursement to costs that grantee actually incurs, which BRI has not shown for the tenant improvements. DCA is thus not applying a "'formalistic' interpretation" of the cost principles that ignores their underlying purpose, as BRI argues.[5] BRI Br. at 14-15, citing DAB No. 18, at 3.

BRI also argues that the Board has held that depreciation or use allowances "are to compensate the grantee for the wear on its facilities, not for any actual outflow of cash," and points out that the improvements it uses in its federally-sponsored research have a definite life span and will have to be replaced. BRI Br. at 10, citing Texas Migrant Council, DAB No. 842, at 3, n.2 (1987); 12-13; BRI Reply Br. at 8. However, in Texas Migrant Council, the grantee had purchased the facilities at issue and thus incurred the costs for which it claimed federal funding. The Board made the cited statement in the context of observing that, as the costs had already been incurred, the grantee could

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[5] The Board also noted that the agency permitted a use allowance on equipment the State provided on the ground that the equipment had been "constructively donated." DAB No. 18, at 2. As we discussed above, the commercial nature of the lease arrangement between BRI and Amgen precludes any conclusion that the tenant improvements were donated to BRI.

spend the federal reimbursement it received without restriction. Id. The issue here is whether BRI may claim depreciation or a use allowance for improvements for which it has not established an acquisition cost.

III. The claimed costs were not determined in accordance with GAAP.

Part 230 requires that claimed costs be determined in accordance with GAAP, and the Department's guidance states that each indirect cost rate proposal "must be accompanied by, and be cross referenced and reconciled to, the grantee's independently audited financial statements which account for all activities during the fiscal year on which the proposal is based." OASMB-5, at 3 (DCA Ex. 1, at 8).

BRI argues that these requirements were met (and that the cost claimed for depreciation or a use allowance was thus properly included in its indirect cost pool), because a note to each of BRI's financial statements in the record reflects the $3,165,000 appraised value of the improvements. BRI points out that the Financial Accounting Standards Board (FASB) has deemed notes to be an integral part of financial statements. BRI Reply Br. at 15-16. Nothing in the note, however, satisfies the requirements of Part 230 or OASMB-5. The note states that the appraised value of the fourth floor improvements had not been recorded in the financial statements. DCA Ex. 4, at 3, 8. BRI concedes that its independent auditors "concluded that in BRI's situation, the assets at issue could not be reflected on BRI's financial statements as depreciable or donated assets." BRI Br. at 9. BRI also acknowledges that "current GAAP standards do not permit BRI to reflect the improvements on its financial statements as depreciable assets" and "do not permit recognition of the improvements as depreciable assets on BRI's financial statements." Id. at 11, 15. Thus, BRI has not shown that it determined its claimed costs for depreciation or a use allowance in accordance with GAAP, as required by Part 230.

Additionally, because BRI's financial statements record no depreciation or use allowance for the improvements, they fail to "account for all activities during the fiscal year on which the [indirect cost rate] proposal is based," as required by OASMB-5.

BRI also asserts that its auditors never concluded that the "transactions were not in accordance with" GAAP, as DCA stated in its letter informing BRI of the determination under appeal. BRI Reply Br. at 2-3, citing DCA Br. at 5, citing BRI Ex. D, at D-2 (DCA determination letter). Any error in the statement in the

determination letter is harmless, however, given BRI's admissions that GAAP do not permit the improvements to be recognized as depreciable assets on the financial statements and that its financial statements do not include costs for depreciation of the tenant improvements.[6]

BRI argues further that the failure of GAAP to recognize BRI's costs for the tenant improvements does not bar federal reimbursement because Part 230 permits depreciation or a use allowance for "certain assets for which no depreciation remains under GAAP accounting standards, or for which no direct costs are booked" by the grantee. BRI Br. at 7, citing 2 C.F.R. Part 230, App. B, ¶¶ 11.b, 11.f.

The Part 230 provisions BRI cites are not applicable. Paragraph 11.f includes the definition of "acquisition cost" for donated assets, which BRI describes as assets "for which no direct costs are booked;" it does not apply to the tenant improvements at issue here, which were not donated. Paragraph 11.b permits a grantee and DCA to negotiate a reasonable use allowance on assets that would be viewed as fully depreciated under the criteria in Part 230, for which no depreciation is otherwise allowed. Even if we agreed that the two provisions BRI cites permit reimbursement of asset costs that GAAP do not recognize (which the provisions do not explicitly state), that would not mean that DCA could not reasonably take into account the requirement that costs be determined in accordance with GAAP in determining whether to permit a use allowance on the tenant improvements at issue here, and certainly would not require DCA to adopt BRI's proposal here based on the 2005 appraised value. Moreover, nothing in those provisions obviates the requirement that a use allowance not exceed two percent of acquisition cost for buildings and improvements, and six and two-thirds percent of acquisition cost for equipment. App. B, ¶ 11.g. Additionally,

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[6] BRI misstates DCA's position as being that "current GAAP standards required BRI to reflect the improvements on its audited financial statements, either as depreciable or donated assets" which, BRI argues, is without support in light of GAAP that "do not permit businesses to reflect many of the liabilities and assets acquired through leases on their financial statements." BRI Br. at 8-9, citing BRI Ex. D, at D-2, BRI Ex. Q (FASB news release). The basis for DCA's determination is that BRI's claimed costs were neither determined in accordance with GAAP nor accounted for in BRI's financial statements. BRI's acknowledgment that GAAP do not permit financial statements to include depreciation of tenant improvements supports DCA's determination.

in determining whether to permit a use allowance, after an asset is fully depreciated, DCA may take into account any factors pertinent to the use of the asset for the purpose contemplated. Id. at ¶ 11.f.

BRI also cites paragraph 11.b as evidence that GAAP support granting a use allowance for the tenant improvements. BRI notes that GAAP call for tenant improvements to be capitalized (by the tenant) over no more than the term of the lease, after which, BRI argues, "there would be no GAAP basis for the landlord to reflect the assets on its financial statements as depreciable assets" and they would thus be fully depreciated assets eligible for a use allowance under paragraph 11.b. BRI Br. at 8. This, BRI argues, "is essentially the situation here, where BRI's independent auditors did not recognize the tenant improvements as depreciable assets upon lease termination." Id. BRI provides no basis to construe the auditors' determination not to recognize the tenant improvements as depreciable BRI assets as meaning that the improvements were fully depreciated and eligible for a use allowance under paragraph 11.b. If anything, the GAAP recognition that tenant improvements are capitalized by the tenant is, like the auditors' determination, consistent with DCA's position that BRI incurred no costs for the improvements eligible for federal reimbursement as depreciation or a use allowance.

BRI also cites a provision permitting depreciation or use allowances on the unamortized portion of equipment in some instances, but that provision by its terms does not apply. The provision states:

> The unamortized portion of any equipment written off as a result of a change in capitalization levels may be recovered by continuing to claim the otherwise allowable use allowances or depreciation on the equipment, or by amortizing the amount to be written off over a period of years negotiated with the cognizant agency.

Part 230, App. B, ¶ 15.b(6) (BRI cites substantively identical language in DCA's "Review Guide for Non Profit Organization's Indirect Cost Proposals," at 29 (BRI Ex. N, at N-9)). The "change in capitalization levels" that paragraph 15.b(6) addresses refers to the increase in the minimum value of equipment that may be capitalized, from $500 to $5,000, that took effect when OMB A-122 was revised in 1998, before its codification at Part 230. 63 Fed. Reg. 29,794, 29,801 (June 1, 1998). The provision thus does not apply to the tenant

improvements at issue here. Even if it did, BRI has provided no information about the extent to which the improvements were amortized or written off during Amgen's tenancy. Equally important, BRI's failure to establish what, if any, acquisition cost it incurred for the tenant improvements for which it seeks federal funding means that depreciation or a use allowance are not "otherwise allowable," as the provision requires.

Conclusion

For the reasons discussed above, we sustain DCA's determination denying BRI's request to include $131,875 for annual depreciation or a use allowance in its indirect cost pool.

/s/
Stephen M. Godek

/s/
Leslie A. Sussan

/s/
Judith A. Ballard
Presiding Board Member