

# **clarification note**

1. Types of link between legal entities and an FCH JU project.
2. Policy on the reimbursement of purchase of equipment

**Approved by the Executive Director 13/05/2014**

## 1. The different types of link between legal entities and a FCH JU project.

Nature of the link	6 Situations	Conditions
A Carry out the project (core tasks)	1 Beneficiary	
B Carry out ancillary tasks	2 Third party carrying some work as <b>subcontractor:</b>	<ul style="list-style-type: none"> <li>• Not core tasks</li> <li>• Not an affiliate</li> <li>• Selected after a transparent and competitive procedure offering best value for money (possibility of pre-existing Framework contract)</li> <li>• Subcontractor is paid a price by the beneficiary</li> <li>• The beneficiary indicates this amount in its form C under direct cost/subcontracting</li> </ul>
	3 Third party carrying out part of the work under <b>special clause 11</b>	<ul style="list-style-type: none"> <li>• Third party linked to a beneficiary               <ul style="list-style-type: none"> <li>○ Affiliates</li> <li>○ Joint Research unit</li> <li>○ European Economic Interest group</li> <li>○ Grouping</li> </ul> </li> <li>• Need to be identified in special clause 11</li> <li>• Third party must fill in its own form C, Certificate on Financial Statement, etc. like a beneficiary</li> <li>• The linked beneficiary will submit together the two forms C and one common report</li> </ul>

<p>C Give access to some resources (staff, research facilities) but remains the owner/controller of these resources</p>	<p>4 Third party making available resources free of charge</p>	<ul style="list-style-type: none"> <li>• Beneficiary does not reimburse the third party</li> <li>• But charges these costs to the projects</li> <li>• Costs to recorded in the accounts of the third party and available for audits</li> <li>• Costs to be declared by Beneficiary <ul style="list-style-type: none"> <li>○ In its FORM C under "other costs"</li> <li>○ In its CFS</li> <li>○ As receipt of the project</li> </ul> </li> </ul>
	<p>5 Third party making available resources and being reimbursed by a beneficiary</p>	<ul style="list-style-type: none"> <li>• Beneficiary reimburses the third party and charges these costs to the projects</li> <li>• Costs to recorded in the accounts of the beneficiary</li> <li>• Costs to be declared in Beneficiary's form c as "other costs" and included in the CFS</li> </ul>
<p>D Sell (lease) equipment. The ownership (or control) of the equipment is transferred from the supplier to the beneficiary</p>	<p>6 Supplier of equipment</p>	<ul style="list-style-type: none"> <li>• Costs to be declared by beneficiary in its form C as "other costs" and included in its CFS</li> <li>• Costs must reflect percentage of equipment used in the project</li> <li>• Costs must reflect depreciation of the equipment.</li> </ul>

## 2. Policy on the Eligibility of Costs for Purchases of Equipment in demonstration projects

**Notion:** Purchase (or lease) of equipment. The ownership (or control) of the equipment is transferred from the supplier to the beneficiary.

### **Principles at stake:**

- *Non-profit principle* which implies that as a general principle the FCH JU reimburses costs rather than prices.
- *Principle of best value for money* which implies that when FCH JU reimburses the price of a subcontractor or a purchase of equipment, it needs reasonable assurance that amounts are not inflated.
- *Operational justifications*: the interpretation of the rules and the degree of flexibility given to a beneficiary should be guided by operational needs (i.e. the success of the project)
- *Consistency and legal certainty* which implies that a beneficiary receives from all the FCH JU actors (staff and auditors) and at all stages of the project (from negotiation to audit) the same answer as regards the eligibility of costs.
- *Cost must be incurred during the project*

### **Background:**

The grant agreement is structured on the idea that the core costs of a project are personal costs while subcontracting and purchases of equipment are ancillary elements. However, in demonstration projects, purchases of equipment (to be demonstrated) may represent a core element of the project and imply large amounts of money.

The grant agreement includes some rules on subcontracting:

- it must be limited to non-core tasks,
- it must be foreseen in the technical annex
- Best value for money must be ensured by procurement rules, or the request of several quotations, or a pre-existing framework agreement.
- Subcontracting is not allowed between two beneficiaries or between a beneficiary and one of its affiliates.

By contrast, the grant agreement (and the financial guidelines) does not contain equivalent rules for purchasing of equipment. It is only said that

- Costs must be declared in form C as “other costs” and included in the CFS
- Costs must reflect the percentage of use of the equipment in the project
- Costs must reflect depreciation of the equipment.

**The question:** In order to comply with the principles at stake, should the subcontracting rules be extended/adapted to purchases of equipment? How should we interpret the depreciation/percentage of use principles in demonstration projects?

**Answer:**

**A. Principle of best value for money:**

For public bodies, best value for money is insured by compliance with public procurement rules.

For private entities, when the purchase of equipment implies high amounts ( $\geq 125,000^1$ ), the FCH JU will apply the same principles as for subcontracting:

1. or request of three offers
2. or a pre-existing framework contract
3. or another detailed explanation of the reasons why only one supplier was possible

In option 2 or 3, it is highly recommended to have a discussion between the FCH JU and the beneficiary to ensure appropriate justification and to document the consent of the FCH JU.

For on-going projects, the implementation of this principle is more sensitive. Indeed the application of the best value for money requirements to the purchase of equipment  $\geq 125,000$  € is not mentioned in the grant agreement and we cannot impose retroactively additional eligibility requirements. Therefore it is recommended to refer to it only when a beneficiary envisages a new purchase of equipment and consults the FCH JU on the procedure to follow.

**B. Purchases from affiliates and other beneficiary**

- Purchase of equipment from another beneficiary or an affiliate under Special Clause 11 (i.e. carrying tasks within the project and providing equipment, case B.3 of the table above): there is no prohibition of transfer of ownership between beneficiaries or affiliates.

The beneficiary may declare the purchasing price provided

- The building of the equipment is not an objective of the project<sup>2</sup>.
- The purchase complies with the rules indicated under the “best value for money” principle.

In cases where an affiliate would not carry tasks but only provide equipment (=> there is no Special Clause 11, case D.6 of the table above): the beneficiary may declare the purchasing price provided the purchase complies with the rules indicated under the “best value for money” principle. For the cases of purchase of equipment, with and without special clause 11, additional evidence on the reasonableness of the “purchasing price” will be requested by the FCH JU, if the following three cumulative conditions are fulfilled:

- (1) the equipment is purchased from an affiliated company of the beneficiary and

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<sup>1</sup> This amount corresponds to the threshold beyond which procurement rules require an open procedure.

<sup>2</sup> if it were the case then the cost of producing the equipment should be declared by the builder of the equipment (and not the price by the beneficiary purchasing it). Maintenance of the equipment when provided by the builder should also be declared by the latter as costs (personnel + other direct cost); when provided by another supplier it should be treated as subcontracting.

- (2) the value of the equipment transferred is above 1/3 of the total costs declared by the beneficiary.
- (3) the purchase of the equipment is project specific (i.e. the purchases made in the project are not a small fraction of a large number of purchases of the same equipment at a standard price between affiliates)<sup>3</sup>

The additional evidence will consist of the breakdown of the total price of the equipment per cost category to assess the reasonableness of the cost components and may include, if deemed necessary by the Authorising Officer, third party invoices of key cost items.

It has to be noted that the additional evidence requested under these cases will be limited in its scope and cannot be assimilated to an audit of the costs components of the 'purchasing price'. The objective of this provision is simply to obtain additional assurance on the respect of the 'best value for money' principle for these specific cases of transactions between affiliates.

The FCH JU will decide, on an ad-hoc basis, depending on (1) the materiality of the total amounts involved and (2) the specific characteristics of the project and of the beneficiaries and affiliates involved, **when** this additional assurance will have to be provided by the beneficiary (i.e. "ex-ante" during the negotiation or the ex-ante review of costs claims vs. "ex-post" through the financial audits in accordance with article II.22 of the grant agreement).

### C. Consistency and legal certainty

For all purchases of equipment ≥125,000, and especially for sensitive cases (cases where the request of three offers is not feasible or when purchase between beneficiaries or between affiliates are envisaged)

- There should be an in depth discussion as early as possible (ideally at negotiation phase) between the beneficiary and the different services of the FCH JU.
- What has been agreed should be discussed with the authorising officer and documented in a note for the file and/or annex 1
- This note should bind all FCH JU actors including the auditors: costs incurred in compliance with what has been agreed and documented will be considered as eligible.

### D. Cost must be incurred during the projects

In the context of the purchase of equipment, the main implications of this principle concern the depreciation rules.

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<sup>33</sup> By analogy with the subcontracting rules, the principle of best value for money is complied with when the purchase is part of a pre-existing (non-project specific) framework agreement.

A beneficiary which purchases equipment is required to comply with the applicable accounting rules. In most cases, the relevant rule requires depreciating the equipment over a given number of years corresponding to the entire economic life of the equipment and the FCH JU will consider as eligible cost the depreciation corresponding to the period during which the equipment was used for the project. For each reporting period, the beneficiary must declare the relevant fraction of the price it paid for the equipment.

In some cases, it may be that applicable accounting rules allow for a quicker depreciation in the context of a R&D project, with for instance a depreciation period corresponding to the duration of the project (i.e. no commercial value/use after the project has finished). After obtaining confirmation that this is indeed in compliance with the applicable accounting rules, the FCH JU will accept the whole price of the equipment as eligible costs. In this situation also the beneficiary must declare for each reporting period, the relevant fraction of the cost incurred for the equipment.

In other cases, it may even be possible that the applicable accounting rules require (or allow) treating the purchased equipment as an asset subject to immediate depreciation (e.g. as a result of the impairment test required by International Accounting Standards if there are indications that the recoverable value is lower than the book value). In this situation, the beneficiary must declare the whole price paid to purchase the equipment in the reporting period corresponding to the payment of the latter. After obtaining confirmation that this is indeed in compliance with the applicable rules, the FCH JU will accept the whole price of the equipment as eligible costs.

In any case, it is advisable to discuss this question of depreciation with beneficiaries as early as possible (ideally during the negotiation process) and in case of quick/immediate depreciation to request explanations on that practice.

