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NIH's New Unilateral Change to Your Institution's Indirect Rate: An Old-School Breach of Contract?

by Alex Hontos, Chris DeLong, and Eric Weisenburger

On Friday, February 7, the National Institutes of Health ("NIH") issued Policy Statement Supplemental Guidance affecting budgets both for active grants and for future grants, which was set to take effect on Monday, February 10 until it was temporarily paused that same day by the United States District Court, District of Massachusetts. If the pause is lifted, the Supplemental Guidance threatens to upend negotiated funding agreements for research institutions and replace them with a flat indirect cost rate for NIH grants, endangering the viability of many research projects and potentially breaching thousands of grant agreements. And Dorsey assesses it probable that other Federal grantmaking agencies (e.g., NSF, DOE, DOD) may follow suit. Clients should take an early opportunity to assess their grant agreements and potential consequences of NIH's sudden policy shift, including reviewing grant agreements for potential breach claims against the government.

What does the Supplemental Guidance do?

There are generally two types of costs in a Federal grant agreement: direct and indirect. Direct costs are those that are directly attributable to the grant-funded project such as researcher salaries and equipment used for the project. Indirect costs (also called "facilities and administration costs") are those that are not devoted to a single project, but are still necessary for it. For example, the depreciation cost of a building that hosts several projects might be an indirect cost, as might administrative support (e.g., compliance costs, accounting costs) not limited to a single project.

Indirect costs in an Institute for Higher Education grant agreement with NIH are typically governed by 45 C.F.R. § 75.414 and 45 C.F.R. § 75 Appendix III (until October 1, 2025, when HHS will adopt 2 C.F.R. § 200 in full with HHS changes to appear in 2 C.F.R. § 300).These principles are commonly incorporated into grant agreements by reference.

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See 45 C.F.R. § 75.210(b).

Indirect costs are typically allowable costs that may be reimbursed at a "rate" set in one of three ways: (1) by statute, regulation, or policy, (2) the "de minimus" rate, or (3) a negotiated rate set by a Negotiated Indirect Cost Rate Agreement between the grant recipient and the agency. Negotiated rates vary widely, from 10% at certain institutions to over 50% at others. And once negotiated, the "negotiated rates must be accepted by all Federal awarding agencies" except "when required by Federal statute or regulation, or when approved by a Federal awarding agency head or delegate based on documented justification" set by regulation.45 C.F.R. § 75.414(c)(1).

NIH's Supplemental Guidance purportedly supersedes existing indirect cost rates even if there was a negotiated rate in place: effective February 10, for "any new grant issued, and for all existing grants to [Institutes of Higher Education] retroactive to the date of issuance of this Supplemental Guidance, award recipients are subject to a 15 percent indirect cost rate." NIH immediately set a flat indirect cost rate for all grants of 15%, for existing and future grants.

What happens next?

On February 10, twenty-two states* sued in the United States District Court, District of Massachusetts seeking injunctive relief under the Administrative Procedure Act preventing NIH from enforcing the Supplemental Guidance for grant agreements taking place in the states that sued. In addition, the Association of American Medical Colleges, American Association of Colleges of Pharmacy, and similar associations brought a parallel case, also in Massachusetts Federal court, seeking the same relief nationwide.

The plaintiff states and plaintiff associations in the two parallel lawsuits ("Plaintiffs") argue that the categorical 15% rate is beyond NIH's statutory authority to set and is an arbitrary and capricious—and illegal—agency action. Specifically, Plaintiffs contend that the NIH did not: articulate a plausible basis for the flat 15% rate, consider Plaintiffs' reliance on the rates already agreed between NIH and the Plaintiffs, justify the 15% rate given the harm it would cause to grant recipients, provide a statutory basis for permitting categorical change to negotiated indirect cost rates or for avoiding binding agreements, and follow a proper agency rulemaking process. For each reason, Plaintiffs argue the Supplemental Guidance is illegal and void.

On February 10, 2025, the United States District Court for the District of Massachusetts granted temporary restraining orders in both cases that stop NIH from "taking any steps to implement, apply or enforce" the 15% rate for a short period.But this is only temporary relief. The hearing on Plaintiffs' requests for longer-term injunctive relief will be on February 21, with a decision likely coming shortly after.

What can institutions do to protect their rights?

Plaintiffs' likelihood of success is uncertain. Should the Court grant longer-term injunctive relief, NIH may continue pushing to reach 15% indirect rate via alternative means,

including seeking to negotiate that rate on current grant agreements and seeking a 15% rate in all future agreements.

Should the Court deny Plaintiffs' motion, though, the Supplemental Guidance will take effect immediately. But that does not mean that recipients are without options. Grant recipients may seek alternative relief in several forms, including potentially bringing claims against NIH at the Court of Federal Claims, a highly specialized tribunal that adjudicates monetary claims involving the Federal government. One potentially viable claim may be breach of the grant agreement if the grant agreement incorporates the negotiated rate and the governing regulations by reference, as most do—it has long been "hornbook law ... that the Government cannot terminate or change one of its contracts in whole or in part without consent of the other contracting party, without being held liable in damages for breach of contract." *Louisiana-Pacific Corp. v. United States*, 228 Ct. Cl. 363, 366, 656 F.2d 650, 652 (1981) (emphasis added). This is "[t]he archetypical repudiation" of a contract—one where the government "attempts to unilaterally alter the contract or to condition [its] performance on terms that were not part of the bargain." *Alaska Pulp Corp. v. United States*, 48 Fed. Cl. 655, 659 (2001).And "[t]he result is no different where the government as a party to the contract commits this same sin through subsequent legislation," or, through a policy statement supplement. *See id.* (citing *Mobil Oil Exploration & Producing Southeast, Inc. v. United States*, 530 U.S. 604 (2000)).

Given the uncertainty of the current injunctive relief in place, a claims assessment for breach is a shrewd move.

Dorsey has deep experience bringing claims against the United States in the United States Court of Federal Claims and advising research and higher-education clients about grant rights and compliance. We are happy to assist clients navigating NIH's sudden and impactful policy—and contractual—changes.

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*The Plaintiff States are Arizona, California, Connecticut, Colorado, Delaware, Hawai'i, Illinois, Maine, Maryland, Massachusetts, Michigan, Minnesota, Nevada, New Jersey, New Mexico, New York, North Carolina, Oregon, Rhode Island, Vermon, Washington, and Wisconsin.