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Costing and Working Capital for Auxiliary and Service Enterprises

<http://www.ucop.edu/ucophome/policies/bfb/a59.pdf>

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Business and Finance Bulletins Home Page: <http://www.ucop.edu/ucophome/policies/bfb/>

I. REFERENCES

- [Business and Finance Bulletin A-47](#), University Direct Costing Procedures
- [Business and Finance Bulletin A-60](#), Short-Term Investment Pool-Distribution of Income
- [Business and Finance Bulletin BUS-43](#), Materiel Management
- [Business and Finance Bulletin BUS-72](#), Establishment and Review of Auxiliary Enterprises

II. INTRODUCTION

The University operates a large number of auxiliary and service enterprises which provide services to other departments or to outside users. These units historically have charged users for their services, and their charges have been set to cover most of their direct costs and some of their indirect costs.

This bulletin prescribes the costs that are to be borne by these enterprises and the related procedures for setting prices, obtaining working capital, and making any necessary settlements with the federal government.

III. DEFINITIONS

Auxiliary Enterprises - Self-supporting activities which provide non-instructional support in the form of goods and services to students, faculty, and staff upon payment of a specific user charge or fee for the goods and services provided (e.g., residence halls, bookstores). The general public may be served only incidentally.

Service Enterprises - Service departments which provide a specific type of service to various institutional departments, rather than to individuals, and which have operating costs supported by recharges to the departments receiving the services (e.g., garages, storehouses).

Direct Costs - Readily identifiable costs associated with the furnishing of goods and services by an enterprise.

Indirect Costs - Costs that cannot be readily identified with or related to a specific enterprise. These costs are related to the services generally provided without charge by central campus units. For the purpose of this bulletin, indirect costs include operation and maintenance of plant (OMP) and campus general administrative services.

IV. REQUIREMENTS

All auxiliary and service enterprises shall be charged for all direct costs involved in producing their goods and services. These costs include salaries and benefits, supplies and expenses, and equipment depreciation, except that depreciation expense will not be charged in bond indentured auxiliary enterprises.

Also, all auxiliary enterprises shall be charged for all indirect costs that are judged to benefit the activities. These costs include those for OMP services such as janitorial, utility, and building maintenance; and for central campus administrative services such as materiel management, personnel, accounting, and environmental health and safety.

V. PROCEDURES

The following procedures shall be established to implement the above requirements:

- A. Account/Fund Assignment - Each auxiliary and service enterprise shall be assigned unique account and fund numbers in the appropriate series in accordance with local campus procedures.
- B. Budget - A budget shall be established for each auxiliary and service enterprise in accordance with local campus procedures.
- C. Direct Costs - All direct costs shall be recorded in the accounts of the enterprise. Direct costs include equipment depreciation expense and any interest expense, except that depreciation expense shall not be recorded for the bond indentured auxiliary enterprises.
- D. Indirect Costs - Indirect costs shall be recorded in the accounts of auxiliary enterprises as follows:
 1. Operation and Maintenance of Plant. The campus Facilities Department shall recharge auxiliary enterprises for all services, using its standard procedures and rates.
 2. Central Campus Administration. Each administrative office which provides specifically identifiable and quantifiable services to an auxiliary enterprise shall recharge for those services. These recharges are to be calculated by deriving a price per unit (e.g., per purchase order, per safety

inspection) and then applying that price to the number of units of service provided.

The various revenue bond indentures governing administration of indentured enterprises specifically prohibit charging them with any share of general administrative expenses of the University (i.e., charges made without regard to services actually and directly provided to such enterprises). Therefore, to document compliance with the indenture covenants, supporting records must be kept (such as actual time records, documents processed, or other tangible evidence) of the specific central campus administration services provided to each indentured auxiliary enterprise.

- E. Prices - Prices are to be established at a level that will provide revenue to cover all direct costs and, for auxiliary enterprises, all indirect costs, after consideration of prior year losses or excess income. Also, prices may be set at a level sufficient to accumulate funds (net worth) required to meet working capital and capital expansion needs. In establishing the pricing structure, the enterprises should take into account any non-operating revenues (subsidy appropriations) which may be available to cover costs. For indentured auxiliary enterprises, prices must also cover debt service and other bond indenture requirements.

All auxiliary and service enterprises shall publish a schedule of rates and prices which shall be reviewed and approved by each campus as part of its annual budget process.

- F. Federal Settlement - Federal costing regulations define certain costs as unallowable as a charge to federal funds. Inclusion of; interest as a direct cost, funds accumulated for capital asset replacement in excess of depreciation on current equipment, and accumulated surpluses will require refunds to the federal government. The federal government will not accept any markup above cost, even if the purpose of that markup is to accumulate funds for equipment replacement or addition or for inventory expansion. Therefore, at the end of each fiscal year, those enterprises which provided services to federally-funded contract and grant activities shall prepare a statement of costs that excludes any interest expenses, accumulation of funds for capital asset replacement in excess of depreciation expense for currently used assets, and accumulated surplus balance in excess of one month of the recharging unit's activity. The difference between such a statement of costs and the revenues actually generated is considered excess pricing by the federal government. The portion of the differential which can be attributed to federal contract and grant activities shall be refunded to individual active grants and contracts or in lump sum to the U.S. Treasury.

There are two alternate ways to comply with federal costing regulations:

1. establish dual-pricing structures for federal and non-federal activities; or

2. instruct federally-funded activities not to make use of certain auxiliary or service enterprises.

G. Working Capital - Financing for current needs of auxiliary and service enterprises such as inventories or accounts receivable, and for capital needs such as equipment, structures, and renovations is to be provided as follows:

1. Capital Needs. Funds for capital needs (above the amount made available by depreciation) may be accumulated by setting prices above costs in order to build reserves, or by borrowing from University or commercial sources. When borrowing from commercial sources, the campus shall first seek financing through lease/purchase, installment purchase contracts, or commercial bank loans to take advantage of the University's ability to borrow on an interest tax-exempt basis. In accordance with Business and Finance Bulletin BUS-43, Materiel Management, Part 8, paragraph II.C., financing through these contracts shall first be cleared with the Treasurer's Office to insure that the campus is receiving a competitive, tax-exempt interest rate.
2. Current Needs. After determining the amount needed to finance inventories and receivables, reserves shall be accumulated and earmarked for this purpose. Borrowing from University funds at market rates can be arranged when the financial plan demonstrates debt service coverage feasibility.

At campus option, accumulated earnings may be transferred to separate reserves to fund the above needs and to fund any refund due to the federal government.

H. Cash Management - Each quarter the average monthly cash balance or cash deficit of auxiliary and service enterprises shall be determined. Interest earned on cash balances or interest charged on cash deficits of these enterprises shall be distributed in accordance with Business and Finance Bulletin A-60, Short-Term Investment Pool-Distribution of Income.