

**New Mexico State University**  
**Internal Service Center Rate Procedures**

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# New Mexico State University Internal Service Center Rate Procedures

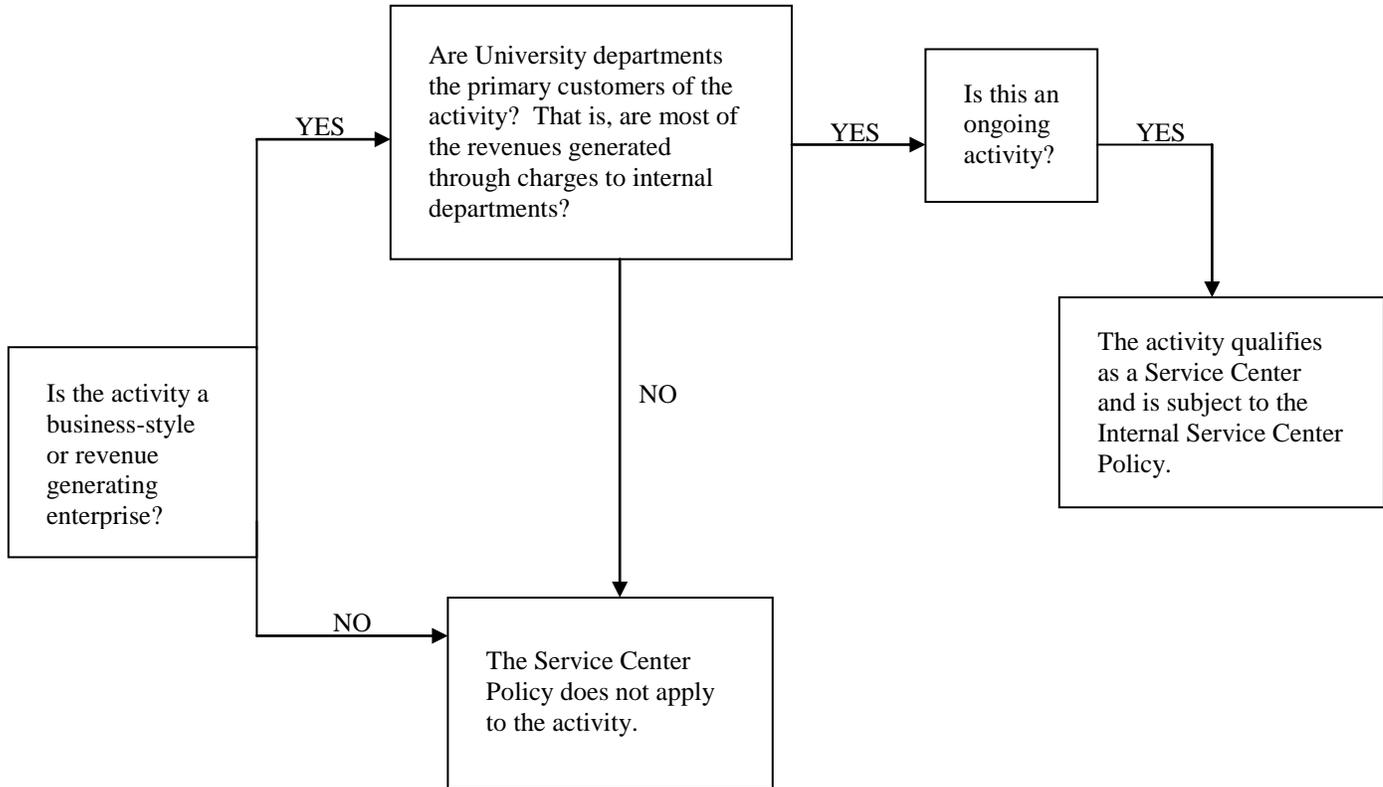
## *Frequently Asked Questions*

### 1. Why justify internal service center rates?

- ◆ Required by Office of Management & Budget ([OMB](#)) Circular A-21
- ◆ Must pass a federal audit for charges to contract and grant accounts
- ◆ To secure funding for NMSU

### 2. How do I know if a service requires an internal service center rate?

Service Centers are operating units established for the primary purpose of providing services to the other university units although services may be provided on an incidental basis to external users. Service Centers are established when management determines that a good or service is most effectively provided within the University, although the same good or service may be available commercially. The purpose of the Service Centers is to control the cost of providing goods/services within the University. The following flowchart provides guidance for determining whether the Service Center Policy applies.



- ◆ Units that only reallocate or transfer certain direct costs, at cost, are not considered internal service centers as defined by this procedure. This includes Departmental Copy Centers that simply allocate out all operating costs. Accounting guidelines can be obtained by contacting the cost accounting office.
- ◆ Departments that operate copy centers are not internal service centers unless they otherwise qualify as defined in Section 2. Accounting guidelines can be obtained by contacting the appropriate Financial Services accounting office.
- ◆ Departments that make infrequent and immaterial interdepartmental sales are not internal service centers. Infrequent sales are sales that do not occur on a regular, on-going basis. To qualify for this exclusion departments must be able to provide documentation showing the interdepartmental sales are infrequent and immaterial.

**3. What is the documentation required for establishing a service center operation?**

- ◆ Internal Service Center Operation Questionnaire ([Exhibit 1](#))
- ◆ Internal Service Center Operation Rate Development Worksheet or a substitute form for each rate.
- ◆ Internal Service Center Rate Summary Sheet that includes all facility rates.

**4. What requirements are service centers are subject to?**

- ◆ Operating accounts for accumulation of direct costs must be established. Costs related to Service Centers should not be co-mingled with other expenses not related to the service function.
- ◆ Service Centers charge other university accounts in accordance with the university account code listing. All credits are recorded in the 795XX series.
- ◆ Billing rates are based on cost and must be applied uniformly to all users. Cost includes direct expenses and current year depreciation as well as over/under recovery from the prior year, although certain items as defined below must be excluded from the rate calculations. In some cases it may be necessary to establish rates at less than full cost, but under no circumstances may rates exceed cost over the accepted operating cycle (approximately five years). Billing rates may not be based on what others charge for similar services. Rates will be calculated on previous 2 years revenue and expenses adjusted for any known variables. For example, FY10 rates will be calculated on FY08 revenue and expenses. If the internal service center continuously operates in a deficit, then the department should perform their own analysis to determine if it's beneficial for the University to continue the service.

**Direct Costs include the following:**

- ◆ Salaries, wages and related fringe benefits
- ◆ Supplies/materials
- ◆ Subcontracts and outside services
- ◆ Other service center operational costs

**Indirect Costs include the following:**

- ◆ Depreciation
- ◆ External interest

**The following costs must be excluded from billing rates:**

- ◆ Capital acquisitions
- ◆ Transfers
- ◆ Debt principal payments and internal interest

The federal government has categorized certain costs as "unallowable" for indirect cost recovery. While these costs may be allowable from University funds, they should not be included in the rate structure for a specialized service facility or a regular service center. These expenses include, but are not limited to, the following categories:

- ◆ Entertainment
- ◆ Bad Debt
- ◆ Advertising
- ◆ Public Relations
- ◆ Alcoholic beverages
- ◆ Contributions and donations
- ◆ Goods or services for personal use

**5. What is working capital?**

- ◆ All Service Centers have a need for a reasonable amount of working capital to manage their cash flow. Therefore, each Service Center is permitted to establish and maintain through its charges a reasonable working capital reserve or cash/cash equivalent, in addition to full recovery of its actual costs. A Service Center may elect to include a working capital reserve in its rate calculation. The maximum allowable reserve is 15% of normal annual operating expenses, reduced by any credit fund balance.
- ◆ The calculation shown below is the most common way to compute a Service Center rate:

$$\frac{\text{(Budgeted Expenses + Prior Year Under-Recover  
or Minus Prior Year Over-Recovery)}}{\text{Total Projected Level of Activity for the Budget Period}}$$

**6. Are transfers out of an operation allowed?**

Service center operations should not transfer revenues, expenditures or fund balances to other activities since such transfers can distort billing rate calculations or alter the break-even plan.

**7. Highlights**

- ◆ Objective of the internal service center is to break even.
- ◆ Method for determining rate: Estimation
- ◆ Types of estimation:
  - prior year actuals
  - expertise and knowledge

- ◆ Objective is to estimate the total annual cost directly chargeable to the service center operation and divide that cost by the total estimated annual utilization units to determine the billing rate per unit. The service center should break even - no surpluses.

## **8. What are Cost Accounting Standards?**

Research institutions must comply with the federal Cost Accounting Standards 501,502,505, and 506. Essentially, these standards promote consistency and uniformity in cost accounting.

The four standards pertain to:

- ◆ consistency in estimating, accumulating, and reporting costs;
- ◆ consistency in allocating costs incurred for the same purposes;
- ◆ treatment of unallowable costs;
- ◆ cost accounting period

Each of these standards is implicit in this policy.

Any questions regarding this policy should be directed to the Cost Accounting and Reporting office at 646-5281 or [car\\_reporting@nmsu.edu](mailto:car_reporting@nmsu.edu).

## **New Mexico State University Internal Service Center Policy**

### **PURPOSE**

To institute a University policy that ensures Service Centers are in compliance with OMB Circular A-21. Internal Service Centers provide services to University departments and generate revenue of more than \$100,000.00.

### **DEFINITIONS**

**Service Center-** A department that performs specific technical or administrative services, primarily for the internal operations of the University and charges users for its services.

**Direct Operating Costs-** All costs that can be directly identified with a service provided by a service center. These costs include the salaries, wages and fringe benefits of University faculty and staff directly involved in providing the service; materials and supplies; purchased services; travel expenses; and equipment rental.

**Indirect Costs-** The costs of administrative and supporting functions of the University such as operations and maintenance of buildings, building and equipment depreciation, space costs, general and administrative expenses.

**Unallowable Costs-** Costs that cannot be charged directly or indirectly to federally sponsored programs. These specific costs are outlined in the Office of Management and Budget (OMB) Circular No. A-21, "Cost Principles for Educational Institutions." <http://www.whitehouse.gov/OMB/circulars/a021/a021.html>

**Equipment-** An item of tangible personal property having a useful life exceeding one year and an acquisition cost of \$5000 or more.

**Billing Unit-** The unit of service given by a service center. Examples include hours of service, machine time used, etc.

**Billing Rate-** The amount charged to a user for a unit of service. Billing rates are usually computed by dividing the total annual costs of a service by the total number of billing units for the period.

**Surplus-** The amount that the revenue generated by a service exceeds the costs of providing the service during a fiscal year.

**Deficit-** The amount that the costs of providing a service exceed the revenue generated by the service during a fiscal year.

## **GENERAL INFORMATION**

Billing rates should be designed to recover the direct operating costs of providing the services on an annual basis. The objective of Internal Service Centers is to break even. No costs other than the costs incurred in providing the services should be included in the billing rates. The calculation should exclude unallowable costs.

All users should be charged for services during the fiscal year the service is rendered. Users should normally be charged the published rates for a service center's services.

Billing rates must not differentiate between federally and non-federally funded users.

All direct operating costs should be charged to the same Index number. Costs not included in the index assigned to the Internal Service Center will not be included in the rate calculation. Documentation to support units of service, billings and rate calculations should be maintained.

Actual cost and revenues should be compared at the end of each University fiscal year. Deficits or surpluses should be carried forward as an adjustment to the billing rates of the following year.

## **CAPITAL PURCHASES**

Expenditures for capital equipment purchases should not be included in the costs used to establish service center rates. Reserves for the purchase of equipment will not be allowed in the calculation of the billing rates, however, service center costs should include depreciation of the equipment used by the internal service center. The inclusion of equipment depreciation in the billing rates will generate funds that will enable service centers to purchase equipment needed in the future. At yearend, the previous year depreciation amount will be transferred to the equipment renewal and replacement (R&R). The transfer to the R&R index at year end will be the responsibility of the department that owns the equipment. The yearend JV should be submitted to Cost Accounting and Reporting with the appropriate backup for approval. Equipment purchases for the internal service center must be made from their R&R account. If the equipment cost exceeds the amount in the R&R account, then the equipment must be financed from other sources of internal unrestricted funding or external financing. A listing of capital equipment, with inventory identification and depreciation amounts, used in services centers can be provided by the Property Accounting Office.

## **BUILDING DEPRECIATION**

The only building related expense that may be included in the internal service center rate calculation is building depreciation. The inclusion of building depreciation in the billing rates will generate funds that will enable service centers to make necessary repairs or new construction needed in the future. At year end, the previous year building depreciation amount will be transferred to the building renewal and replacement (BR&R). Building repair or construction for the internal service center must be made from their BR&R account. If the repair cost exceeds the amount in the BR&R account, then the building construction must be financed externally

## **ESTABLISHMENT OF NEW SERVICE CENTERS**

The establishment of new service centers must be approved by the Cost Accounting and Reporting Office. The request for a new Internal Service Center must contain the following information:

A description of the services and the users of the services is to be provided.

Proposed revenue and expenses for the next year.

Type of Utilization used (hours, number of individuals served)

Billing rate calculations with supporting data. CAR will work with the department to assist in the development of billing rates.

CAR will review for reasonableness and methodology within 10 business days. With CAR's approval the department can implement the new rate immediately. The rate will be reviewed in 6 months to determine if the rate is appropriate.

## **REVIEW OF SERVICE CENTERS**

Cost Accounting and Reporting will conduct periodic review of the financial operations of service centers. These reviews will focus on the development of billing rates, handling of surpluses and deficits, and the adequacy of the service center's record keeping procedures. Cost Accounting and Reporting will review and approve annually any rates for internal service centers with annual revenue greater than \$1 million. Any new rates or changes in existing rates for internal service centers with annual revenue between \$100,000 and \$1M will need to be reviewed before implementation of the new or revised rates. If no change in the rates for these service centers occurs, they will be reviewed every two years. Cost Accounting and Reporting will review the fund balances of all Internal Service Centers at the beginning of each fiscal year. Service centers with significant deficits or surpluses will be subject to review, regardless of annual revenue.

Internal service centers meeting the review criterion will need to have the rate proposals to cost accounting and reporting no later than December 31 for approval of the next fiscal year's rates.