

This document reflects the result of analyses, discussions and review by UCOP staff and PricewaterhouseCoopers (PwC) to date. The document is subject to change pending additional discussions with PwC; however, it represents the best information available to date.

## **University of California GASB 35 Depreciation Reporting**

### **Issues Resolution Memo No. 20**

#### **Approach to Recharge Centers**

##### **Define Issues**

The University must establish guidelines for the consistent treatment and reporting of equipment in recharge centers (includes specialized service facilities and other recharge activities).

##### **Background**

During 1999, the Government Accounting Standards Board (GASB) introduced GASB Statements 34 and 35. Among other matters, these Statements will require the University to account for depreciation in its financial statements for the fiscal year beginning July 1, 2001, with comparative information for the prior year. Financial statements must be prepared in accordance with Generally Accepted Accounting Principles (GAAP) and are subject to audit under Generally Accepted Auditing Standards (GAAS).

Recharge centers are operated as self-supporting units. The recharge rates are based on the cost of operations, including depreciation expense of equipment used by the recharge operation. The recharge rates are subject to review by campus review procedures.

Issues Resolution Memo (IRM) No. 16, *University Useful Lives*, established that University useful lives must be consistently and uniformly applied for financial reporting purposes (University and medical centers), Medicare cost reports, F&A cost rate proposals, and recharge centers. Therefore, the University must establish a Useful Life table that provides a uniform and systematic approach that can be defended to internal and external auditors, including the federal government.

Within the context of a single Useful Life table, the University seeks a process that provides recharge centers the flexibility to manage their operations.

## **Recommended Approach**

- The University has established a Useful Life table to be used throughout the institution.
- For purposes of reporting depreciation in the consolidated financial statements, the University will depreciate recharge center equipment based on the useful lives established in the University Useful Life table.
- Recharge centers (includes specialized service facilities and other recharge activities) are encouraged to use the useful lives set forth in the University Useful Life table when developing their recharge rates.
- There may be cases where the use of the Useful Life table may present operational problems for recharge centers. In such cases where there is a variance between the University Useful Life table and operational experience, the following alternatives may be considered:
  1. Recharge centers may apply lives based on their specific experience for a particular piece of equipment in a specific setting. All non-standard useful lives used in recharge rate proposals must be substantiated and are subject to approval in accordance with campus recharge rate review policies. That is, recharge centers would be responsible for documenting the circumstances that require a useful life that is different from the average useful life provided in the University Useful Life table. The documentation and campus review process are subject to audit by PricewaterhouseCoopers (PwC).
  2. In using the life from the University Useful Life table, recharge centers may consider the residual value of equipment in the development of recharge rates. (The University assumes the residual value for equipment is zero for financial statement purposes.)

### *Example—*

- Fleet Services purchases a vehicle that costs \$20,000.
- The current useful life listed on the Useful Life Table is 4 years.
- Equipment Management records the vehicles at \$20,000, with a useful life of 4 years and a salvage value of \$0. The annual depreciation expense reported in the financial statements will be \$5,000.
- However, Fleet Services determines that the residual value for the vehicle is \$8,000. For purposes of developing the recharge rate only, the depreciation expense is calculated as follows:

$$\frac{(\$20,000-8,000)}{4 \text{ years}} = \$3,000 \text{ per year}$$

- Depreciation expense of \$3,000 per year will be taken by the recharge center until the vehicle's disposal, or until the entire \$20,000 has been depreciated.

- The appropriate gain or loss will be recorded upon disposal by the recharge center.
- 3. In using the life from the University Useful Life table, campuses may allow planned deficits for recharge centers for some years with offsetting surpluses in other years in order to achieve stability in recharge rates. This depends on local campus recharge center policy and such decisions should be made in consultation with campus Budget Offices.
- 4. Campuses may petition UCOP–Financial Management to consider finer gradations in equipment classifications on the Useful Life table.
- This policy will take effect January 1, 2002 for new equipment purchased by recharge centers and included in recharge rates for FY 2001-2002. Equipment purchased before January 1, 2002 may continue to be depreciated using the useful lives currently established by the recharge centers.

#### *Advantages*

- Consistent with the UCOP’s stated goal of maintaining a uniform depreciation approach for various purposes: University financial statements, medical center financial statements, Medicare Cost Report, F&A cost rate proposals.
- Consistent application of the University Useful Life table will provide a systematic and rational approach that can be defended to internal and external auditors, including the federal government (i.e., DHHS–Division of Cost Allocation).
- Provides recharge centers with flexibility to manage their operations based on their experience.

#### *Disadvantages*

- Campuses must ensure proper review and approval of all recharge activities on the campus and will be subject to audit by PwC.

### **Next Steps—Required Actions**

- OP will seek concurrence with the recommended approach at the November North/South campus meetings at UC Irvine.
- Campuses should review the current draft of the University Useful Life table with their major recharge centers to determine whether additional gradations are desired. Campuses should notify OP by January 31, 2001.
- During 2001 (January through December), campuses may request additional equipment classifications that are identified through the recharge rate proposal approval process.