

University of Pennsylvania School of Medicine
Policy & Procedure Manual

SERVICE CENTER EQUIPMENT & DEPRECIATION

Financial Administration
Policy Number: FA – FIN – 001
Date Approved: 09/23/2009
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I. PURPOSE

To establish procedures for charging depreciation expense to Service Centers for capital equipment and using the recovery of depreciation to replace Service Center equipment. To comply with University of Pennsylvania financial policy and procedures, particularly [Sponsored Projects Policy No. 2115](#), *University Service Centers* and federal costing standards relevant to sponsored programs, including Office of Management and Budget (OMB) Circular A-21 ([2 CFR, Part 220](#)).

II. POLICY STATEMENT

- Capital equipment purchases for equipment to be used in a Service Center **cannot** be charged directly to a Service Center account (i.e. 26-digit account number with the following *ORG 47XX* and *Fund 000011* combination).
- Depreciation expense calculated for the use of the capital equipment by the Service Center may be included as a direct operating cost when formulating the Service Center rates.

Note: If you purchase equipment for use by a Service Center directly from federal sponsored project funds, you may **not** include the depreciation of this equipment in the Service Center rates.

- A capital reserve account will be established for Service Centers that have been approved to include depreciation expense in their annual operating costs used to calculate the billing rates. Service Center rates should be set with the objective to break even (i.e. revenues less expenditures netting to zero), whether depreciation expense is included or excluded.

The capital reserve account will be funded based on the actual amounts of depreciation expense charged each fiscal year. Use of this account will be restricted to offset the cost of future capital purchases for the Service Center, and pay for repairs or maintenance to existing Service Center equipment.

III. WHO SHOULD KNOW THIS POLICY?

Individuals responsible for financial management of Service Centers in the School of Medicine, including business administrators, scientific directors or center directors, department chairs, Service Center managers or supervisors, and any other interested parties responsible for financial operations or oversight of Service Centers in the School of Medicine and in University central offices, such as the Director of Cost Analysis in the Office of Research Services.

IV. DEFINITIONS

Break-even—when revenue equals expenses, whereby there is no variance between the two; prohibiting a surplus (revenue greater than expenses) or a deficit (expenses greater than revenue).

Capital Equipment—Equipment to be capitalized refers to an item of non-expendable tangible personal property with 1) a useful life of more than one year; 2) a cost in excess of \$5,000 per item; excluding freight charges and taxes; and 3) the University has title to the asset. Equipment may be moveable or fixed. In addition, acquisitions of individual items of software with an acquisition cost of \$5,000 or more will be considered a capital asset.

Depreciation—a decline in value of an asset because of use, wear or obsolescence. The purpose of depreciating assets is to have the value of the assets in the accounting system reflect its likely market value over the life of the asset.

Depreciation Expense—amount expensed each accounting period to reduce the value of an asset in the accounting system. The accounting transaction does *not* involve a use of cash.

Service Center—a broad term to define an operating unit within the School of Medicine that provides goods or services for a fee based on a rate schedule, to recover no more than the cost of the goods or services and to break-even over time. Some Service Centers can be further classified as the following:

- **Recharge Center**—a Service Center that provides routine, non-specialized services based on a rate schedule, to recover no more than the cost of the goods or services and to break-even over time (e.g. a copy center or glass-washing center would be considered a Recharge Center).
- **Research Core Facility**—a highly complex or specialized Service Center designated by the School of Medicine as a core facility.
- **Specialized Service Facility**—as defined by OMB Circular A-21; a Service Center that provides highly complex or specialized facilities, generally with an annual budget over \$1,000,000 and significant charges to federal projects (i.e. 50% or more).

Straight-Line Method—a common and fairly simplistic method to calculate depreciation expense, by starting with the purchase price of an asset and dividing it by the useful life of the asset to arrive at the annual depreciation expense. This is charged each accounting period in equal installments until the book value of the asset (value in the University General Ledger) is reduced to zero (the expected market value of the asset at the end of the useful life of the asset). For example, assuming a \$25,000 piece of equipment has a 10 year useful life, the depreciation expense calculation is as follows:

$\$25,000$ (purchase price) / 10 years (useful life) = $\$2,500$ (annual depreciation expense)

Useful Life—the estimated life of equipment determined by the University Comptroller's Office Property Management Group based on established asset capitalization Category Codes¹ that is recorded into the Property Management System.

¹ University of Pennsylvania, Office of the Comptroller, Property Management Group, Category Codes found online at: <http://www.finance.upenn.edu/comptroller/accounting/property/propcodes.shtml>

V. GENERAL INSTRUCTIONS / PROCEDURES

In order for a capital reserve account to be established and funded, the following must occur whenever capital equipment is purchased, leased (capital leases only), or transferred to a Service Center:

1. Capital equipment has been entered into the University of Pennsylvania Property Management System,
2. Service Center must submit a request to the School of Medicine, Department of Finance (SOM Finance) that includes the following information:
 - Item description,
 - Penn barcode number,
 - Purchase Order (PO) number,
 - Annual depreciation expense² and depreciable life of the asset (as it appears in the Property Management System),
 - Any changes in useful life of the equipment (as it appears in the University Property Management System), or notification of sale or disposal of the equipment, needs to be communicated to SOM Finance.
3. Depreciation expense must be included into the Service Center billing rates,

SOM Finance will forward the annual depreciation expense amount to the Office of Research Services. A journal entry will be processed by SOM Finance at the end of each quarter to recognize the depreciation expense that should be charged to each Service Center, along with recording the corresponding depreciation revenue recovery. The revenue will be transferred to a capital reserve account to fund future Service Center equipment purchases, using the following journal entry:

Debit (DR.) 400-47xx-1-000011-5340-0000-0000 (Service Center Account)

Credit (CR.) 400-47xx-2-014001-5340-0000-0000 (Capital Reserve Account)

Each fiscal year, the Service Center must provide SOM Finance, with the following information:

- List of all approved capital equipment used in the Service Center,
- Amount of depreciation expense to be expensed to the Service Center in the upcoming fiscal year,
- Appropriate ORG code, and
- Total depreciation amount that will accumulate over the useful life of the equipment.

² Calculate depreciation using the straight-line method, which is an equal amount over the useful life of the equipment. To calculate, start with the book value of the asset divided by number of years in the useful life, which equals the annual depreciation expense. Here is an example to demonstrate how to calculate depreciation expense for a \$25,000 piece of equipment with a 10-year useful life; $\$25,000 \div 10 = \$2,500$ depreciation expense per year.

VI. ADDITIONAL PROCEDURES

Restrictions on Use of Capital Reserve Account

The capital reserve account, (400-47xx-2-014001-5340-0000-0000), will be restricted to the following:

1. The capital reserve account must only be used to replace equipment used in the Service Center and the funds must *not* be transferred to any other ORG codes.
2. The revenue *cannot* be used to offset or eliminate deficits in the Service Center.
3. As long as the equipment is being used in the Service Center, the Department must depreciate the equipment until the end of its useful life and include annual depreciation expense in the Service Center rates.
4. Any proceeds generated from the sale or disposal of Service Center capital equipment must be credited to a departmental special purpose account.
5. When closing a Service Center, use of any balance in the capital reserve account will require authorization from the School of Medicine, Department of Finance.

The capital reserve account funds may only be used for the purposes outlined in this policy. Annual depreciation will be placed in the capital reserve account whether the Service Center has a surplus or deficit throughout the year. No other types of credit entries can be made to the capital reserve account other than depreciation journal entries outlined in this policy.

VII. RELATED POLICIES AND RESOURCES

- Financial Policy Manual, *Accounting Policy No 1106.0 through 1106.7, Plant Assets*, found online at: <http://www.finance.upenn.edu/vpfinance/fpm/1100/1106.0.asp>
- Financial Policy Manual, *Sponsored Projects Policy No. 2108, Cost Accounting Standards (CAS)*, found online at: <http://www.finance.upenn.edu/vpfinance/fpm/2100/2108.asp>
- Financial Policy Manual, *Sponsored Projects Policy No. 2110, Federal Direct Cost Expenditures*, found online at: <http://www.finance.upenn.edu/vpfinance/fpm/2100/2110.asp>
- Financial Policy Manual, *Sponsored Projects Policy No. 2111, Unallowable Costs*, found online at: <http://www.finance.upenn.edu/vpfinance/fpm/2100/2111.asp>
- Financial Policy Manual, *Sponsored Projects Policy No. 2115, University Service Centers*, found online at: <http://www.finance.upenn.edu/vpfinance/fpm/2100/2115.asp>
- Financial Policy Manual, *Sponsored Projects Policy No. 2116, Facilities and Administrative (F&A) Costs*, found online at: <http://www.finance.upenn.edu/vpfinance/fpm/2100/2116.asp>
- Office of Management and Budget, Circular A-21, *Cost Principles for Educational Institutions*, found online at: http://www.whitehouse.gov/omb/circulars/a021/a21_2004.html
- University Office of Research Services, *Sponsored Projects Manual, Chapter 17 Service and Recharge Centers*, found online at: <http://www.upenn.edu/researchservices/Manual.html>
- School of Medicine Department of Finance, online Service Center information: <http://www.med.upenn.edu/finance/centers.html>

VIII. CONTACTS

Responsible Offices for School of Medicine Service Centers		
Research or Scientific Inquiries	Financial Management Inquiries	Compliance Inquiries
Office of the Executive Vice Dean and Chief Scientific Officer 354 BRB II/III / 6160 Philadelphia, PA 19104 Telephone: (215) 898-2874 Fax: (215) 573-7945 http://www.med.upenn.edu/vdresearch	Department of Finance 356 Anatomy-Chemistry Bldg / 6061 Philadelphia, PA 19104 Telephone: (215) 898-3190 Fax: (215) 898-1174 http://www.med.upenn.edu/finance	Office of Research Compliance and Integrity 240 John Morgan Bldg Philadelphia, PA 19104 Telephone: (215) 573-3125 Fax: (215) 573-7945 http://www.med.upenn.edu/comply

ISSUED BY: _____ DATE: _____

Vice Dean for Administration and Finance