

AUXILIARY ENTERPRISES

Contents

	<u>Page</u>
I. Introduction	2
II. General Description of Auxiliary Enterprises	2
A. Definition	3
B. Establishment of an Auxiliary Enterprise	2
C. Types of University Auxiliary Enterprises	2
D. Administration of Auxiliary Enterprises	4
III. Financing of Auxiliary Enterprises	4
A. Financing of Construction	5
B. Financing of Operations	6
IV. Accounting for Auxiliary Enterprises	6
A. Accrual Accounting	6
B. Income	7
C. Expense	7
D. Net Income and Accumulated Earnings	8
V. Responsibilities	10
VI. References	11
Exhibit A	12

AUXILIARY ENTERPRISES

"Take time enough: all other
graces will soon fill up their
proper places."

-- John Byrom

I. INTRODUCTION

This chapter provides a general description of auxiliary enterprises and a list of the types of enterprises operated for the University. It also describes the financing arrangements available for funding the construction of these activities and the accounting procedures for certain transactions.

II. GENERAL DESCRIPTION OF AUXILIARY ENTERPRISES

A. DEFINITION

An auxiliary enterprise, as defined by the National Association of College and University Business Officers (NACUBO) in the College and University Business Administration manual, is "an entity that exists to furnish a service to students, faculty, or staff, and that charges at a rate directly related, but not necessarily equal, to the cost of the service." Auxiliary enterprises are 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 that is at least equal to the full direct and indirect cost of providing the goods and services. The general public may also be served incidentally by some of the enterprises. Although the operation of an auxiliary enterprise is supplemental to the primary educational functions of the University, such enterprises are important to the overall operation of the University.

B. RATIONALE FOR ESTABLISHMENT AND OPERATION OF AUXILIARY ENTERPRISES

Prior to the establishment of an auxiliary enterprise, the need for such goods or services must be identified which, if provided at a reasonable cost and at a convenient location, would enhance and support the University's instructional, research, or public service programs. The plan to provide these goods or services through a University-operated or affiliated auxiliary enterprise must take into account the availability, the price, and the quality of any such goods or services offered by the local business community. If it is anticipated that the enterprise may generate unrelated

business income, e.g., related to the sale of goods and services to the general public, the potential tax liability also must be considered in planning and budgeting for the activity (see Exhibit A for President Gardner's memo on University Policy on Activities Generating Unrelated Business Income). When such goods or services are reasonably available under favorable commercial terms and conditions, the determining factor in the decision to operate a particular auxiliary enterprise must be the demonstration of the greater benefit that would accrue to the instructional, research, or public service programs of the campus from University operation of such an enterprise.

C. TYPES OF UNIVERSITY AUXILIARY ENTERPRISES

Examples of auxiliary enterprises are housing operations, non-housing food service operations, parking operations, bookstores, student centers/unions, and child care centers. Following is a summary of the types of auxiliary enterprises operated on University campuses:

1. Student, Family, and Faculty Housing and Dining Facilities

This group is classified into two categories:

- a) University of California Housing System (UCHS) facilities which operate within the context of a Bond Indenture (issued for the legal protection of the bond holders who have provided financing for construction of the facilities); and
- b) Campus Housing Facilities, which include all other housing that is not declared part of the facilities in a) above.

2. Student and Staff Facilities

Student and staff facilities include recreational facilities, student stores, and child care centers.

3. Parking Operations

Parking systems are classified as auxiliary enterprises on all campuses. The systems are financed from parking fees collected from students, faculty, and staff.

4. Student Centers/Unions

Student unions are financed primarily by their revenue producing activities.

5. Intercollegiate Athletics

Intercollegiate athletics at Berkeley and Los Angeles, for example, are classified as auxiliary enterprises because of the substantial receipts generated through sales to the general public. At campuses where athletics involve only student participation, athletic programs are classified as "organized activities" or as part of the department of physical education.

6. Physician's Offices, Museum Stores, and University Airport

These three enterprises, which are financed primarily by their revenue producing activities, are not operated on all University campuses.

Although hospitals serve students, faculty, and staff, they are classified separately and produce their own financial statements because of their financial significance and because they serve a teaching function.

D. ADMINISTRATION OF AUXILIARY ENTERPRISES

1. Systemwide

The Associate Vice President--Business and Finance provides executive direction to the Office of the President (OP) Financial Planning and Analysis Office and is responsible to the Senior Vice President--Administration for establishing and maintaining policies and procedures related to auxiliary enterprises.

2. Campus

The Vice Chancellor--Administration at each campus is responsible for the business management functions of auxiliary enterprises, such as budget control and the receipt, custody, and disbursement of revenues; accounting and financial reporting; and procurement of supplies, equipment, and services. The directors and managers of enterprises that are primarily business or service oriented are generally responsible to the Vice Chancellor-Administration. Directors and managers

of enterprises that are primarily educational generally are responsible to an academic administrative officer. Each campus, however, approves its own organizational hierarchy; the authority delegated to particular officers may vary from campus to campus.

III. FINANCING OF AUXILIARY ENTERPRISES

Many auxiliary enterprises have debt service commitments that must be repaid from enterprise revenues. The enterprises may borrow funds for the construction of facilities either from sources outside the University or from The Regents. These borrowed funds must be repaid from enterprise revenues. (The general policy of The Regents stipulates that funds made available for the construction of facilities are subject to repayment, usually with interest.)

Funds also may be borrowed from The Regents or other campus enterprises to finance on a temporary basis auxiliary enterprise inventories, equipment purchases, or other assets. These obligations are also required to be repaid from enterprise revenues.

Reserves are accumulated to replace facilities or equipment to ensure that the facilities are operated on a continuous basis. Provisions for replacement are funded from enterprise revenues.

Following is a more detailed outline of the various types of financing available to auxiliary enterprises.

A. FINANCING OF CONSTRUCTION

For the construction of capital facilities, revenue producing enterprises may borrow capital funds to be repaid from operations. Capital facilities also may be constructed with financing to be repaid from student fees. In all such cases, borrowings must be supported by evidence of the ability to meet debt service requirements and other financial obligations. The sources of borrowed capital are either external, from bank loans and revenue bonds, or internal, from Regents advances. Loan proposals are reviewed by the Associate Vice President--Business and Finance. Following administrative approval, projects requiring financing are submitted by the President to The Regents for final approval. (Refer to Business and Finance Bulletin BUS-55, Financing Feasibility of Loan Projects, for additional information.)

1. Sale of Bonds

The University issues revenue bonds as one means of providing funds for the construction of auxiliary enterprise facilities. This type of funding is used for the construction of housing and parking facilities, student centers/unions, and student and staff facilities. Debt repayment is made from the net revenues of the facility or from specific fees assessed and collected for this purpose. Each bond indenture, however, specifically states the pledged repayment source.

2. Advances to Projects

Advances in the form of Regents' loans are made to finance the construction of an auxiliary enterprise project or the purchase of property. These advances, made from such funds as the University Opportunity Fund, or Nuclear Science Fund, must be repaid over a period of years with interest from project revenues. The interest rates, which may vary, are generally related to the bank prime rate in existence at the time the advance is made.

3. Other Sources

Other sources of funds for auxiliary enterprise construction include private donations and special State appropriations.

B. FINANCING OF OPERATIONS

All current assets of auxiliary enterprises reduced by accounts payable should be funded by their current fund balances, or their reserve funds when an immediate need for these funds is not foreseen. However, since most enterprises begin operations without funds and may require working capital to fund inventory and/or receivables, the following sources of funds are available for this purpose.

1. Interfund Borrowing

Working capital may be borrowed from other funds on the same campus, as outlined in Accounting Manual chapter C-173-13, Cash: Balances of Individual Funds. Approval of an interfund loan for an outstanding working capital loan must be obtained from the campus Vice Chancellor--Business and Finance.

2. Regents' Working Capital

If funds are not available locally, a request for a Regents' Working Capital loan can be submitted to the office of the Associate Vice President and Director of the Budget.

Generally, the purpose of such loans is to provide interest-free advances of working capital to finance inventories, receivables, and equipment. The funds must be repaid over a specified period of time. The amount of the loan is reported under the liability line-item "Due to Regents' Working Capital" in the current liabilities section of the enterprise balance sheet.

IV. ACCOUNTING FOR AUXILIARY ENTERPRISES

A. ACCRUAL ACCOUNTING

The accounting procedures for auxiliary enterprises are similar to those used in commercial enterprises; financial statements are prepared on an accrual basis. Although accruals and deferrals are taken into account for management reporting purposes, such items are not recorded in the general ledger until June 30.

B. INCOME

Auxiliary enterprise activities should generate sufficient funds to cover all their operating expenses, debt repayment obligations, repayment of advances from Regents' Working Capital, and to provide reserves for the long-term maintenance of facilities and the replacement of equipment.

1. Income From Sales and Services

Auxiliary enterprises receive income primarily from charges for sales and services to students, faculty, and staff. In some instances, income may be received from the general public. In addition, such activities may occasionally provide services to University departments; the costs for these services are recovered through interdepartmental recharges.

2. Sales of Assets

The receipt of funds from the sale of auxiliary enterprise assets is recorded as income, rather than as an addition to current fund balances.

3. Non-operating Income

Income received by auxiliary enterprises from sources other than regular operational service charges is accounted for as non-operating income. Non-operating income typically includes gifts and endowments, incidental fee allocations, and other special allocations.

C. EXPENSE

Expenditures for auxiliary enterprises are recorded in the functional category 76XXXX. Such expenditures include the cost of salaries and wages, employee benefits, supplies and services, rentals, reserve accrual, repairs, telephone, utilities, equipment and facilities, plant operation, maintenance, etc.

Supplies and materials purchased for operating inventories are recorded during the fiscal year in expenditure accounts under the sub-account classification "Stores" or "Materials for Sale." At June 30, when all charges and accruals to these expenditure accounts have been recorded, a reversing entry is made to transfer the total amount of the physical inventory to the inventory balance sheet account. The balance remaining in the expenditure accounts then represents the cost of goods sold during the fiscal year. For additional information on inventory adjustments, refer to Accounting Manual chapter I-581, Inventories.

D. NET INCOME AND ACCUMULATED EARNINGS

The net income of auxiliary enterprises for the fiscal year is added to accumulated earnings at June 30. UCHS accumulated earnings are recorded at OP in Retirement of Indebtedness Funds 01712. These accumulated earnings can be used to fund other non-operating costs or transfers. With the approval of the Associate Vice President--Business and Finance, these funds can be used for other campus purposes. For example, the following accounting procedures should be used when UCHS funds are transferred for UCHS Major Maintenance Projects and when advanced for student center construction:

1. UCHS Major Maintenance Funds

In order to fund UCHS major maintenance projects, OP transfers UCHS Major Maintenance Funds to each campus at the time the allocation is approved by the Associate Vice President--Business and

Finance. The following accounting entries are made to record this transfer:

Financial Journal:

Dr. UCHS Revenues J-101712-01712-X-5100
Cr. OP Spec Fin Control 1-119517

Treasurer's Financial Journal:

Dr. OP Spec Fin Control J-119518-090010
Cr. Campus Fin Control J-1195X0-0900X0

Campus:

When the campus receives this journal with a copy of the approval letter, the following entries are made:

Dr. OP Fin Control X-119500
Cr. UCHS Net Revenue X-101712-01712-X-5100

The funds can be retained in this account or moved either to Renewals and Replacement Funds using a transaction code 3400, or to Current Funds using transaction codes 3030 and 0540.

Short Term Investment Pool (STIP) income earned on these funds is recorded in the UCHS Net Revenue fund at the OP. For STIP control purposes, the following additional fund numbers are reserved by OP in Renewals and Replacement Funds and Current Funds:

Renewals and Replacement Funds 76640 to 76649
Current Funds 70520 to 70529

Expenditures can be recorded using a single fund number or a different fund number for each year or type of project. The campus can charge Current Funds or Renewals and Replacement Funds during the year, then at year end transfer the funding from fund X-01712. The campuses are responsible for managing these funds.

UCHS funds that are not spent within three years are considered lapsed. Lapsed or surplus funds must be returned by October following the fiscal year in which the funds have lapsed or are determined to be surplus. To return these funds to OP, the journal entries used to transfer the funds should be reversed (see section above). OP journals must be sent to Corporate Accounting.

2. UCHS Loans for Student Centers/Unions Construction

When OP transfers UCHS funds for the construction of student centers/unions, the University is lending funds to an outside entity. The following accounting entries are made to record this transfer:

Financial Journal:

Dr. UCHS Revenues J-101712-01712-X-5100
Cr. OP Spec Fin Control 1-119517

Treasurer's Financial Journal:

Dr. OP Spec Fin Control J-119518-090010
Cr. Campus Fin Control J-1195X0-0900X0

Campus:

The following entries are made in response to the transfer of funds from OP:

Dr. OP Fin Control X-119500
Cr. UCHS Revenues X-101712-01712-X-5100

The following entries are made to record the disbursement of funds to the student centers/unions:

Dr. UCHS Revenues X-101712-01712-X-2998
Cr. Campus Cash X-110XXX

The following entry establishes the receivable and payable in a Retirement of Indebtedness Fund:

Dr. UCHS Advances X-101606
Cr. UCHS Payable X-101696

Payments from student centers/unions should be deposited in the campus UCHS Net Revenue Fund 01712. Interest payments are recorded using a transaction code 1305 and principal with a transaction code 1998. The following entry also is made to reduce the principal payment payable and receivable accounts:

Dr. UCHS Payable X-101696
Cr. UCHS Advances X-101606

At year end, the funds are transferred to OP as follows:

Dr. UCHS Revenues X-101712-01712-X-5100
 Cr. OP Fin Control X-119500

The following OP journal entries are made to show the amount of principal and interest:

Financial Journal:

Dr. OP Spec Fin Control 1-119517
 Cr. UCHS Revenues J-101712-01712-X-5100

Treasurer's Financial Journal:

Dr. Campus Fin Control J-1195X0-0900X0
 Cr. OP Spec Fin Control J-119518-090010

V. RESPONSIBILITIES

The accounting officer is responsible for ensuring that the procedures detailed in this chapter are followed.

VI. REFERENCES

Accounting Manual Chapters:

A-115-17	Accounting Procedures for Acquisition and Sale of Service Enterprise Assets
A-115-18	Accounting Procedures for Funding Current Working Capital Requirements of Service Enterprises
C-173-13	Cash: Balances of Individual Funds
I-581	Inventories

Business and Finance Bulletins:

A-17	Housing and Food Service Operations Uniform Cost Accounting System
BUS-55	Financial Feasibility of Loan Projects
BUS-72	Establishment and Review of Auxiliary Enterprises

College and University Business Administration manual

Historical note: Original Accounting Manual chapter first published 10/1/73. Revised 6/30/96; analyst--Ken Strangfeld.

Exhibit A

