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**Coded Memo: FS 2016-01,
supersedes FS 2011-05**

Date: March 18, 2016

To: Assistant Vice Presidents and Financial Officers' Association Delegates

From: Mary Ek, Assistant Vice Chancellor/Controller

Subject: Definition of Major (Non-recurring) Maintenance & Repair Costs as Used in Executive Order 994 and Chapter 15 of the *Legal Accounting and Reporting Manual* - **UPDATED**

Dear Colleagues,

In 2011, guidance was requested in connection with the definition of “major” maintenance and repair costs as used in Executive Order (EO) 994 since the term “major” was subject to varying interpretations throughout the CSU. The prior version of this memo, FS 2011-05, was intended to provide information to assist in the achievement of system-wide consistency in the recording of these costs. The definition affected the selection of CSU fund for posting these costs and the calculation of the debt service coverage ratio (DSCR).

This update has been prompted by the inclusion of a new chapter in the [Legal Accounting and Reporting Manual, Chapter 15, Capital Projects – Funding for University Facilities](#). Chapter 15 addresses the accounting aspects of the spending authority granted by the California legislature in connection with both deferred maintenance and new construction projects. It introduces new terminology in connection with repair and maintenance costs and changes both the nature and the descriptions of certain CSU funds.

Section 2.7 of EO 994 states: “For a Project or Program Extraordinary Expenses and Major Maintenance and Repairs will not be included in the DSCR . . .”; Chapter 15 applies different terminology so that “major” maintenance and repair costs are referred to as “non-recurring”. “Recurring” maintenance and repair costs are those that are “routine”. See Chapter 15 for complete definitions of “recurring” and “non-recurring” maintenance and repair costs. “Recurring” repair costs are included in the DSCR to evaluate financial viability of capital projects by CSU management; “non-recurring” repair costs are excluded from the calculation.

DSCR is a standard financial analysis calculation used to evaluate the ongoing cash flow strength of a program or entity with debt service obligations. As the financing market prescribes, the calculation is based on current period revenue and expenditures, not based on reserves, in order to measure an entity’s ability to generate cash from operations on a consistent basis. The higher the DSCR, the more favorably an entity is viewed by investors and rating agencies.

“Non-recurring” maintenance and repairs are not synonymous with capital expenditures. Capital expenditures are costs incurred to acquire or construct a capital asset, defined in Chapter 13 of the GAAP Reporting Manual as “. . . real or personal property that has a unit acquisition cost equal to or greater than \$5,000 and an estimated life greater than one year.” The cost of “recurring” maintenance and repairs should be recorded either in auxiliary enterprise operating funds or in the CSU operating fund, if the expenditure pertains to academic or administrative buildings. The cost of “non-recurring” repairs should be recorded either in auxiliary enterprise repair and maintenance funds or in the academic repair and maintenance fund, if the expenditure pertains to academic or administrative buildings. The choice of an appropriate CSU fund is important since it is used as the identifier to distinguish between “recurring” maintenance and repairs and “non-recurring” maintenance and repairs.

For your reference, below is a listing of auxiliary enterprise operating funds, repair and maintenance funds, and academic program funds¹ in state fund 0948 that are used in the calculation of the DSCR:

Operating Funds (to record "recurring" maintenance and repair)			
Program	SCO Fund	CSU Fund	Description
Academic	0948	485	TF CSU Operating Fund
Housing	0948	531	TF Housing-Operations and Revenue
Student Union	0948	534	TF Campus Union-Operations and Revenue
Parking	0948	472	TF Parking Revenue Fund-Parking Fees
Health Center	0948	452	TF Facility Revenue Fund-Health Facilities Fee
Continuing	0948	441	TF Extended Education Operations
Maintenance and Repair Funds (to record "non-recurring" maintenance and repair)			
Program	SCO Fund	CSU Fund	Description
Academic	0948	486	TF-Academic Maintenance & Repair
Housing	0948	532	TF-Housing Maintenance & Repair
Student Union	0948	535	TF-Campus Union Maintenance & Repair
Parking	0948	474	TF-Parking Maintenance & Repair
Health Center	0948	454	TF-Facility Maintenance & Repair
Continuing Education	0948	443	TF-Extended Education Maintenance & Repair

¹ “Academic Program” in the context of maintenance and capital improvements, the subject of Chapter 15, is defined to include academic and other non-self-support facilities, such as administration buildings, library and classrooms.

Additionally, below is a listing of auxiliary enterprise and academic capital improvement funds. Only capital improvement expenditures should be recorded in these funds.

Capital Project Funds (to record capital expenditures)			
Program	SCO Fund	CSU Fund	Description
Academic	0948	487	TF-Academic Capital Improvements
Housing	0948	533	TF-Housing Capital Improvements
Student Union	0948	536	TF-Campus Union Capital Improvements
Parking	0948	473	TF-Parking Capital Improvements
Health Center	0948	453	TF-Facility Capital Improvements
Continuing Education	0948	442	TF-Extended Education Capital Improvements

Regarding the choice of object codes, object code 660021, Repairs & Maintenance, is available to record both “recurring” and “non-recurring” repairs as well as both building and equipment repairs. Because this object code is no longer associated with a specific FIRMS program code, the department in which the expense is recorded will determine the FIRMS program code to which it is derived (i.e., based on Rule 4, the department ID). Object code 660021 is the only choice when recording repairs and maintenance in operating funds, however, other object codes for non-capital expenditures may be used in the maintenance and repair funds if they more accurately describe the nature of the expenditures (e.g., 613001, etc.). Capital project expenditures should be recorded in the object code series 607XXX.

Ultimately, the classification of a repair and maintenance item as either “recurring” or “non-recurring” is a matter of judgment and will vary depending on the campus size and the nature of the repair. It is critical that a careful evaluation of the classification of each repair expenditure be made to ensure the accuracy of the DSCR. EO 994 establishes minimum values that must be met for the campus’s debt program. Falling below these benchmarks could jeopardize the campus’s ability to finance future projects.

The attachment to this memo provides an example of inappropriate recording of non-recurring (major) maintenance and repair expenses and an example of appropriate recording of these costs, with a demonstration of the impact of each on calculation of the DSCR.

The effective date of this document is July 1, 2016. Should you have any questions, please feel free to contact Roberta McNiel at 562-951-4668 or Sedong John at 562-951-4577.

Cc: Chancellor’s Office Financing and Treasury, FSAC Members, CPDC

Example of Inappropriate Recording of Non-recurring M&R Expenses and Impact to Debt Service Coverage Ratio (DSCR)

	Object Code	Amount
Revenue		
Sales and Services of Auxiliary Enterprise	504000	6,500,000
Interest from SMIF	507001	80,000
Other Operating Revenues	580090	1,500
Total Revenue		6,581,500
Expenses		
Management and Supervisory	601201	1,000,000
Support Staff Salaries	601300	100,000
Benefits	603000	650,000
State prorata	612001	180,000
Chancellor's Office	660025	40,000
Services from Other Funds/Agencies	617001	400,000
Supplies and Services	660003	1,500,000
Maintenance and Repair (Recurring M&R)	660021	60,000
Total Expenses		3,930,000
Net Income		2,651,500
Debt Service		2,750,000

In this example, Non-recurring M&R Expenses totalling \$1,200,000 were incorrectly recorded as Supplies and Services.

Debt Service Coverage Ratio (DSCR)	0.96
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The DSCR is understated and does not meet the minimum requirement of 1.10. If M&R had been recorded properly, the DSCR would be 1.40.

Transfer to M&R Reserve	250,000
Transfer to Construction	100,000
Transfer to Catastrophic Event Reserve	500,000
Net Income <u>after</u> debt service and transfers	(948,500)
Beginning Balance	5,550,000
Ending Balance	4,601,500

Reserve Funds

M&R Reserve

Beginning balance	3,500,000
Transfer in	250,000
Expenditures	0
Ending balance	3,750,000

The Non-recurring M&R expenses totalling \$1,200,000 that were incorrectly recorded as Supplies and Services under Operating Expenses and should have been recorded here.

Construction Reserve

Beginning balance	1,500,000
Transfer in	100,000
Expenditures	-
Ending balance	1,600,000

Catastrophic Event Reserve

Beginning balance	2,500,000
Transfer in	500,000
Expenditures	-
Ending balance	3,000,000

Example of Appropriate Recording of Non-recurring M&R Expenses and Impact to Debt Service Coverage Ratio (DSCR)

	Object Code	Amount	
Revenue			
Sales and Services of Auxiliary Enterprise	504000	6,500,000	
Interest from SMIF	507001	80,000	
Other Operating Revenues	580090	1,500	
Total Revenue		6,581,500	
Expenses			
Management and Supervisory	601201	1,000,000	
Support Staff Salaries	601300	100,000	
Benefits	603000	650,000	
State prorata	612001	180,000	
Chancellor's Office	660025	40,000	
Services from Other Funds/Agencies	617001	400,000	
			Appropriate M&R Expense which does NOT include Non-recurring M&R.
Supplies and Services	660003	300,000	
Maintenance and Repair (Recurring M&R)	660021	60,000	
Total Expenses		2,730,000	
Net Income		3,851,500	
Debt Service		2,750,000	
DSCR		1.40	Appropriate DSCR which meets minimum benchmark of 1.10.
Transfer to M&R Reserve		250,000	
Transfer to Construction		100,000	
Transfer to Catastrophic Event Reserve		500,000	
Net Income <u>after</u> debt service and transfers		251,500	
Beginning Balance		5,550,000	
Ending Balance		5,801,500	
<u>Reserve Funds</u>			
M&R Reserve			
Beginning balance		3,500,000	
Transfer in		250,000	
Expenditures		1,200,000	Appropriate Recording of Non-recurring M&R Expense.
Ending balance		2,550,000	
Construction Reserve			
Beginning balance		1,500,000	
Transfer in		100,000	
Expenditures		-	
Ending balance		1,600,000	
Catastrophic Event Reserve			
Beginning balance		2,500,000	
Transfer in		500,000	
Expenditures		-	
Ending balance		3,000,000	

Prepared by: Financing and Treasury
May 4, 2011