Commercial Activities – Operational Guidelines for 2010

This document consolidates information provided at ET and VCAC as well as information provided as part of the budget process, and explains what will be different in accounting for Commercial Activities from 2010.

The changes establish a cleaner approach to enable genuine surpluses from Commercial Activities to be reinvested by those making them. The key changes are:

- Only activities that are run to generate surpluses will be treated as Commercial
- Surpluses from Commercial Activities have been disaggregated from Faculty's operating budget, i.e. faculties retain and reinvest all surpluses generated, after fully accounting for all costs
- Surpluses are measured after fully accounting for both direct and indirect costs

Existing balances representing genuine surpluses will continue to carryover and be available for spending in the future, but still within the context of faculties managing within a net breakeven for Commercial Activities.

Why changes are required

Clearer Definition of Commercial Activities	• To remove a lot of unnecessary administrative work, e.g. moving balances between fund types • To facilitate the application of a set of business rules which better meet the needs of Faculties, Schools and Centres

Surpluses from Commercial Activities disaggregated from Faculty's operating budget	• To remove the confusion that has led to expectations that prior year surpluses could be accessed again (i.e. spent twice)
	• To provide better incentives for faculties (schools, centres and individuals) to generate a surplus that can be reinvested in supporting teaching and research.
	  ○ Previously commercial activities were included in a Faculty's Unrestricted results, therefore effectively having to provide a return of 35-55% to avoid the faculty from cross-subsidising out of its operating budget.
	  ○ Disaggregating commercial activities from the Faculty Operating result ensures any genuine surplus is available to reinvest

Surpluses measured after fully accounting for costs	• To provide more transparent information on the performance and cost of various activities. This will assist Faculties in making better resource allocation decisions *Note that Faculties may choose to undertake non profit-generating activities for many good reasons – marketing, community engagement, student experience etc. They do not need to be dressed up as commercial activities to do this.*

Defining Commercial Activities

Currently many research and operating activities are inappropriately handled through Commercial Activities. In many cases this is because the finance systems have (until now) disallowed invoices being raised except through Commercial projects. From 2010, activities will be accounted for more appropriately as follows:

- Commercial: Activities run with the intention of generating a surplus
- Operating: All activities in Divisions[1] previously accounted for as Commercial, and for faculties, activities which are integral to teaching and research, and ancillary and support services which are not run to make surpluses.[2]
- Restricted: Activities where the revenue is more appropriately classified as beneficial, or where it directly funds or arises from research (taking HERDC eligibility as defining a research income stream)

[1] Divisions' role is to provide services supporting teaching and research, and operate on a net cost basis. To the extent that any of their activities generate revenue, that revenue reduces the net cost of their services – it does not drive incremental expenditure. Accounting for some Division activities as 'Commercial' therefore serves no purpose.

[2] Rebasing adjustments made in setting 2010-2012 operating budgets include an estimate of activities that will be defined as Operating rather than Commercial Activities from 2010. The adjustment provides an uplift to faculty operating budgets so that faculties are not disadvantaged in 2010 by managing additional activities within those operating budgets.

Appendix A sets further guidance for assessing where activities should be accounted for.

Treatment of surpluses from Commercial Activities

- The principle for Commercial Activities is that all genuine surpluses made are reinvested in teaching and research by the faculty making them.
- Surpluses from any particular activity could be spent before they are realised, in the year they are realised, or in a later year. However, **at a faculty level** surpluses made and surpluses spent must achieve a net balance – preferably annually, but if that cannot be achieved over a budget triennium. i.e. in managing to budget faculties must deliver a result that is breakeven or better across Commercial Activities in aggregate.

Each faculty may develop its own internal guidelines to help manage timing differences between the generation and spending of surpluses. For example, each budget unit may be required to manage to breakeven or better on an annual basis, or unders and overs may be balanced at a faculty level.

Measuring surpluses: Activities must be fully costed

Fully costed means two things: that a contribution to indirect costs has been allowed for, and that direct costs have been fully attributed. Details on the application of direct and indirect costs are set out in the UNSW Policy on Competitive Neutrality and Pricing, and are summarised below:

- Direct costs are directly attributable to the project, and may include salaries and on-costs of project staff, stipends of research assistants, materials and supplies etc.
- Indirect costs are the University's costs that cannot easily be allocated to single projects. They include the provision and maintenance of physical infrastructure, insurance, legal and financial management services, and information resources and telecommunications.
- Indirect costs are difficult to attribute and to quantify, and are applied as a simple formula across all projects (a percentage of each project's gross revenues)[3]

Further details on how indirect costs will be applied in 2010 are set out in Appendix B.

Project memorandum balances

Commercial Activity projects are a recording and reporting tool, which enable a record to be kept of the life to date transactions recorded to each project. Project balances do not represent assets to the University. They are simply a memorandum record.

Legacy issues exist with respect to current Commercial Activity "balances" that appear in memorandum records used by schools, centres and individuals. These balances represent funds that have already been counted as part of Faculties' unrestricted results, and thus already spent within Faculties. However, there are substantial expectations among schools, centres and academics that these balances can be spent again. Two things have contributed to these expectations:

- Although the project accounts are a memorandum system, they have been presented as representing real cash balances, available for spending in addition to any approved annual budget allocation
- Representations have been made to some schools, centres and individuals that balances in these accounts are 'theirs', and are unrelated to the faculty annual result

Options for managing these legacy issues were discussed at ET and VCAC in October 2009. The agreed approach is that faculties should honour expectations around access to those memorandum balances which

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[3] For 2010 the contribution to indirect costs has been set at 15% for all activities, which is probably low. More work will be done on an appropriate rate in the longer term, with the intention of developing two rates – one for on campus activities and an off campus rate.

represent legitimate surpluses, but will need to do this within the context of managing profit generation and spending to a net breakeven.

To assist faculties manage this dual role, finance will support a clean-up process to confirm which of the memorandum balances represent legitimate surpluses. Those balances which represent legitimate, fully costed Commercial Activity surpluses will continue to carryover.

The clean-up process is described in Appendix C. *Ultimately it will be the responsibility of the Director of Finance, after consultation with faculties, to confirm which balances represent genuine surpluses.*

Transitioning to the new arrangements

From 2010, activities will be managed as projects within restricted, operating or commercial as described in Appendix A.

In addition, genuine memorandum balances will be re-aligned with how activities will be managed from 2010 as summarised in Appendix C.

- Memorandum balances for activities that are to be managed as restricted will be transferred to restricted funds (likely Q1 2010)
- Memorandum balances that represent genuine surpluses on Commercial Activities will remain as carried forward balances in Commercial Activities
- Memorandum balances which do not represent genuine surpluses on commercial or restricted activities will be cleared, after consultation with faculties.

Note that there are some 2000 project account balances to be reviewed; therefore this process will continue through Q1 2010

Further Information

Please contact Mathew Vial via your Finance Manager.

Appendix A: Guidelines on where specific activities should be accounted for

Activities should be accounted for as:

<table>
<tr><td>Operating</td><td>Activities which are integral to teaching and research such as field trips, course materials etc.
Ancillary support services from which there is no objective to generate a profit, for example BRC</td></tr>
<tr><td>Commercial</td><td>Activities undertaken with the intention of generating a surplus</td></tr>
<tr><td colspan="2">There will be occasions when it is not clear cut as to whether an activity should be classified as Operating or as Commercial. Typically, a service that is primarily performed to generate income and which is also provided to students at a discount is likely to be considered commercial.</td></tr>
<tr><td>Restricted</td><td>Activities where the revenue directly funds or arises from research, taking HERDC eligibility as defining a research income stream (RF222). This includes research activity conducted via UNSW Global
The faculty share of Royalties from Intellectual Property commercialised through NSi (RF222)
Where funds received from external parties have a constructive obligation as to their use, they may be best accounted for as beneficial funds. This is likely to apply in very limited circumstances, and will need to be discussed with Foundation Office to ascertain the appropriate treatment</td></tr>
</table>

The table below provides <u>an indication</u> of where activities are likely to be accounted for in 2010, based on current GI fund codes. Ultimately, however, it is the nature of the activity which determines the classification, not the current fund code. For example, some fund types include a mixture of operating and commercial activities e.g. conferences. To minimise the administrative burden for Faculties finance will arrange a bulk transfer of Projects based on the classifications below. Finance will liaise with Faculties to realign Projects which have incorrectly categorised through this process.

Activities conducted by Divisions only		**Faculty Operating Activities**		**Faculty Commercial Activities**		**Mixed Activities**	
Activities conducted by Divisions only; all activities in this fund code will be remapped so that they are accounted for in Operating activities in 2010.		Activities conducted by Faculties which in most cases will be accounted for as Operating Activities in 2010. These activities will be remapped to Operating.		Activities conducted by Faculties which in most cases will be accounted for as Commercial Activities in 2010. These activities will remain in Commercial.		Fund type is used for both Commercial and Operating activities. Activities will initially remain classified as Commercial, and will be reviewed on a case by case basis with Faculty management to determine which should be realigned.	
GI101	Admissions Revenue	BA001	Continuing Educ, Seminar	GI106	Educational Tech	GI105	Conference
GI103	Careers & Employment	BA101	Working Account	GI127	Publications	GI117	IT Services
GI107	Environment Activities	GI102	Animals	GI129	Short Courses	GI118	Lab Commercialisation
GI112	Housing/Accomm	GI104	Course Materials	GI131	Software Sales	GI123	School Outside Earnings
GI113	Health Licence Fees	GI108	Exhibition/Perf	GI132	Outside Teaching		
GI114	Health Vaccine Sales	GI109	Field Trip/Stud Camp	GI136	Workshops		
GI115	Investment Income	GI110	Graduation Sales	GI130	Faculty Facility Hire		
GI116	Int'l Students	GI121	Marketing				
GI119	Library Fines	GI122	Sale of Course Notes				
GI120	Library	GI134	Bridging Courses				
GI125	Parking						
GI126	Post Office						
GI128	Rentals						
GI133	Unigym						
GI135	Unisuper/Mgt Fees						
GI137	Din & Staff Dining						
GI139	Commissions						
GI111	Facility Hire (Divisions)						

Appendix B: Full costing guidelines

Direct costs

Direct costs are those costs that are directly attributable to the project and may include salaries and on-costs of project staff, stipends of research assistants, materials and supplies etc.

Salary costs are usually the main direct costs that are incurred in Commercial Activities. UNSW has well established practices for apportioning direct salary costs across multiple fund categories and/or cost centres. This is effected using the FSD09 & FSD10 forms.

In order to apply direct costs against Commercial Activities, you will need to complete the relevant FSD09 or FSD10 form to apportion direct salary costs across multiple fund categories and/or cost centres.

Indirect Costs

Indirect costs will be charged at 15% of revenues. Finance is investigating ways of streamlining the process, so that where possible the indirect costs are processed (via journal) when the invoice is raised.

The indirect costs will be credited to a central account. This is because the vast majority of University overheads are incurred centrally and not charged to faculties (e.g. space, utilities, and facilities).

Note re Other Overhead Levies

Note that indirect cost deductions from contract research (the 30% contract research levy) and from activities managed through controlled entities will be credited to faculty operating accounts. These amounts have not been taken into account when setting faculty operating budgets; therefore they represent an additional income stream for the faculty. This enables the Dean to continue to exercise discretion over the use of these monies (i.e. to invest, directly or indirectly, in the individual/school/centre that undertook the activity).

Appendix C: Clean up of current Memorandum Balances (Faculties)

The objective of the clean-up is for Faculties to confirm the Commercial Activity project balances that satisfy the criteria to be treated as Memorandum Balances carried forward into 2010. At a minimum these balances must represent a genuine (i.e. fully costed) surplus from externally funded commercial activities.

The need to conduct this exercise is to avoid balances that have been generated under erratic and inconsistent accounting practises being mixed with truer results generated under full costing rules. It would not be appropriate to divert monies away from current strategic priorities to honour balances that do not represent genuine surpluses.

Finance will liaise with management in each faculty to establish an appropriate review process, based on the number and value of balances to be investigated. Faculties will be asked to nominate a representative to coordinate the review.

The initial analysis involves:

- Review of all large (>$500k) or a-typical balances
- Running a reasonableness test over all balances (over $5k) to identify which should be subject to further review. Indicators of balances that might not represent fully-costed surpluses include:
  - Inter-fund transfers of revenues
  - Balances without any charges for indirect costs
  - Balances with little or no expenditure (including people costs) charged against revenue
  - Balances with a significant lapse of time between the crediting of revenue and charging of expenditure

Any balances identified, in the initial analysis, as potentially not being genuine surpluses will need to be reviewed by the Faculty to determine the true nature of the transactions and therefore the recommended action. The recommended action should also take into account any related debit balances.

At the end of the process the Faculty will make recommendations, consistent with the approach endorsed by VCAC, to the Director of Finance as to which balances should carry forward. Once the Director of Finance has approved the balances for carry forward, other balances will be cleared.

Summary of proposed treatment for existing Commercial Activity memorandum balances

Scenario:	
Activities transferred to Operating	Memorandum project balances will not carry-forward
Activities remaining in Commercial Activities	Balances that represent genuine surpluses will continue to carryover and be available for spending, but still within the context of faculties managing within their budget envelope for Commercial Activities overall.
Activities transferred to Restricted	Balances that represent genuine surpluses will be transferred and will continue to carry forward.
Levy account balances from GI accounts	Do not represent surpluses from Commercial Activities and therefore there is no legitimate expectation that balances will be carried forward. These balances will be cleared.
Levy account balances from contract research	These may represent legitimate expectations as to amounts available to be spent by Schools and Centres. Finance will liaise with each Faculty to arrange the most appropriate treatment of these balances.