

# **ATTACHMENT B**

**APPLICATION OF INDIRECT COSTS TO THE CALCULATION OF FEES FOR  
SERVICES**

## Attachment B: Application of Indirect Costs to the Calculation of Fees for Services

The purpose of this exhibit is to provide a detailed explanation of the methodology used by the City of Newport Beach to incorporate indirect overhead costs in the development of the municipal fee schedule. The nature of indirect overhead costs will also be described. A Fire Department, Fire Prevention Special Event Permits - Public Display - Fireworks Aerial Display Fee (Fee) facilitates the explanation.

The 4<sup>th</sup> of July and Boat Parade are wonderful opportunities for people to enjoy spectacular fireworks shows right here in our own community. An incredible amount of time and energy goes into planning, preparing, inspecting, and ensuring that these events go smoothly. Safety is paramount. The permit application submitted to Fire Prevention must include proof of liability insurance, State Fire Marshal licenses, and a list of persons working the shoot. The Fire Life Safety Specialist reviews the packet and provides a list of "Conditions" to the applicant to follow upon approval. The day of the shoot, the Fire Life Safety Specialist does an onsite



inspection in the morning, afternoon, and evening to ensure all safety requirements are met and verifies the pyrotechnician has their license and double checks its validity. The Fire Life Safety Specialist is present during the show and after checking for possible fires, extinguishing fires should they occur, stopping the show at any time if necessary, and ensuring that all debris is cleaned up. The following steps demonstrate how the Fee is derived.

### Step 1: Calculate Hourly Staffing Rates and Burdened Factors

The first step is to determine the hourly rates of staff providing the services associated with the fee. Table 1 below provides the hourly salary and benefit rates plus the hourly burdened factors for the staff that are responsible for performing this task within Fire and Community Development Department (CDD). Indirect overhead costs or "burdened factors" are costs that are not directly accountable to the expenses incurred for a user fee service, but are necessary and contribute to the total cost of that service delivery, i.e. - managerial administration, utilities, insurance, legal, information technology, payroll, and finance, which are all valid components to the analysis of what it costs the City to provide municipal services.

**Table 1- Hourly Rates for Salary, Benefit and Overhead Factors**

	Salary and Benefits Hourly Rate		Burdened Factors Hourly Rate		Total Burdened Rate
Fire Life Safety Specialist II	\$100.54	+	\$96.53	=	\$197.07
CDD Permit Tech	\$75.97	+	\$84.04	=	\$160.01
Fire Marshal	\$108.99	+	\$104.64	=	\$213.63

The City's cost allocation plan consultant uses the Federal Office of Management and Budget (OMB) Super Circular 2 CFR Part 200 as a guideline to determine the allowable burdened, or indirect, cost elements. The Super Circular is a document that state and local governments use to identify

allowable indirect costs when applying for reimbursement of cost from state or federal programs. Although the calculation of user fee services is not specific to applying for reimbursement from any state or federal program, the underlying methodology of identifying costs is much the same. The relevant sections of the Super Circular that specify how direct and indirect costs shall be applied to the calculation of the Fee follows below.

## Composition of Cost

### Direct Costs

1. General. Direct costs are those that can be identified specifically with a particular final cost objective.
2. Application. Typical direct costs include:
  - a) Compensation of employees for the time devoted and identified specifically to the performance of the operation.
  - b) Cost of materials acquired, consumed, or expended specifically for the purpose of fulfilling the mission of the operation.
  - c) Equipment and other approved capital expenditures.<sup>1</sup>
  - d) Travel expenses incurred specifically to carry out the operation.

Using the personnel identified in Table 1, the direct costs for the public display of aerial fireworks greater than ten minutes are found on line 1.1 (total salary and benefits on an hourly basis) in Table 1a below.

**Table 1a**

Fully Burdened Hourly Rates			Fire Life Safety Specialist II	CDD Permit Tech	Fire Marshal
Annual Salary & Benefits:			\$ 209,121	\$ 158,016	\$ 226,691
1. Calculate hourly salary & benefits					
1.1 Divide annual cost by 2,080 hrs			\$100.54	\$75.97	\$108.99
<b>Total Salary and Benefits</b>	<u>Fire</u>	<u>CDD</u>	<b>\$100.54</b>	<b>\$75.97</b>	<b>\$108.99</b>
2. Indirect Overhead					
	<u>Prevention</u>	<u>Building</u>			
2.1 Compensated Absences (vacation, sick leave)	13.4%	13.4%	\$13.47	\$10.18	\$14.61
2.2 General Administration (supervision, support services)	27.025%	37.146%	\$27.17	\$28.22	\$29.45
2.3 Operating Expense (training, supplies, maint & repair)	24.765%	21.959%	\$24.90	\$16.68	\$26.99
2.4 Citywide Overhead (Finance, City Manager, Human Resources)	30.818%	38.123%	\$30.99	\$28.96	\$33.59
<b>Total Indirect Overhead</b>	<b>96.0%</b>	<b>110.6%</b>	<b>\$96.53</b>	<b>\$84.04</b>	<b>\$104.64</b>
<b>Total Burdened Rate:</b>			<b>\$197.07</b>	<b>\$160.01</b>	<b>\$213.63</b>

<sup>1</sup> Includes maintenance and/or depreciation expense only, not equipment purchases, which are capitalized over a number of years.

## Indirect Costs

1. General. Indirect costs are those: (a) incurred for a common or joint purpose benefiting more than one cost objective, and (b) not readily assignable to the cost objectives specifically benefitted. The term “indirect costs,” as used herein, applies to costs of this type originating from staff within Fire Prevention and CDD Building, their operating expenditures and administration support, as well as those incurred by administrative departments in supplying goods, services, and facilities.

The cost of service analysis includes four types of indirect overhead categories or “cost pools” consisting of compensated absences, general administration, operating expenses, and citywide overhead.

- a) Compensated Absences – The compensated absences cost pool is used to account for employees' time off with pay for vacations and sick days. The City is obligated to pay for these days off and is required by the matching principle to record the expense when the employees are working, since the benefits are a part of the employees' compensation. It is estimated that 280 out of 2,080 total available hours per year per full-time equivalent (FTE) are taken as compensated absences. This translates into a 13.4% burden factor applied to the hourly salary and benefit rate as indicated on line 2.1 in Table 1a above.
- b) General Administration – The general administration cost pool includes the cost of staff time spent on such activities as budget planning and staffing allocations; public counter and telephone time, meetings, and training and education. The wages of management staff and the workers engaged in administration and support activities are considered an indirect labor cost. It is calculated that 27% of Fire Prevention and 37.1% of CDD Building's overall workload is spent on this general administrative function as indicated on line 2.2 in Table 1a above.
- c) Operating Expenditures – The operating expenditure cost pool consists largely of Internal Service Fund (ISF) charges to the divisions on a cost reimbursement basis. The City's internal service funds are used to allocate the cost of providing general liability insurance and workers' compensation; maintaining and replacing the City's rolling stock fleet; and the cost of maintaining and replacing the City's computers, printers, copiers, and telecommunication services. This cost pool also includes other general operating expenses such as publications, supplies, and training. The operating expenditure burden factor of 24.8% for Fire Prevention and 22% for CDD Building as indicated on line 2.3 in Table 1a above is calculated by comparing the total cost of (allowable indirect) operating expenditures to the total (allowable direct) labor pool.
- d) Citywide Overhead - The Cost Allocation Plan (CAP) distributes the costs of City departments that serve a central service function supporting MOD and Revenue operations. These “Central Service Departments/Divisions” include: City Council, City Clerk, City Manager, Finance & Treasury Financial Planning, and Financial Reporting, as well as Human Resources Risk Management. The citywide overhead burden factor of 30.8% for Fire Prevention and 38.1% of CDD Building is calculated by comparing the total cost of Fire Prevention and CDD Building's share of citywide overhead to the total (allowable direct) labor pool (see line 2.4 in Table 1a above).

## Step 2: Calculate Time Spent on the Service

The second step is to calculate the time spent on the service. The task and time in minutes estimated to complete the task is captured in Table 2 below.

**Table 2: Task Description & Time Estimates in minutes**

	Review application, conduct inspections morning, afternoon, and evening day of event	Schedule and Verify Code Compliance	Process and File Permit
Fire Life Safety Specialist II	280 minutes		
CDD Permit Tech		1 minute	
Fire Marshal			10 minutes

## Step 3: Calculate the Cost to Provide the Service

The third and final step is to calculate the cost to provide the service by converting the total minutes to hours per unit (or staff person). The product of the hourly rate calculation times the time spent yields the cost of providing the service (see Table 3 below).

**Table 3 – Fee is Product of Times and Rates**

	Total Minutes		Total Hours per Unit		Fully Burdened Hourly Rates		Total Cost to Provide the Service
Fire Life Safety Specialist II	280.00		4.667		\$197.07		\$919.66
CDD Permit Tech	1.00	➡	0.0167	X	\$160.01	=	\$2.67
Fire Marshal	10.00		0.1667		\$213.63		\$35.61
							\$957.93
					<b>Proposed Fee</b>		<b>\$957.00</b>

## Summary

The purpose of a CAP is to accurately, fairly, and reasonably distribute the City's central administrative costs to the operating departments in the City. The development of a CAP follows a series of general guidelines and principles, which originate from federal guidelines established in OMB Super Circular. These principles ensure that allocated costs are necessary and reasonable to the operation of the government. A cost analysis study is almost entirely reliant upon the data provided by the City. Since all study components are interrelated, bad data at any step in the process will cause the ultimate results to be flawed. To avoid accuracy problems and other quality flaws, the study included a series of quality control measures including reasonableness tests and validation; balance and cross checks; and internal City review. Finally it should be noted that private businesses typically add a layer of profit margin to their cost analysis, public agencies are not allowed to do so.

