

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, using the Harbor Department, Special Event Permit – Simple fee as the example.

Permitted special events held on the waters of Newport Harbor allow for an array of unique organized programs and activities to take place in the bay. Sailing race events, rowing regattas, fishing tournaments, and anchorage raft-up activities are just a few examples. In order to ensure that a special event can take place safely and successfully, staff collects information about the scope of the event, time, dates, and other important event details. The Harbor Department staff will review details of the program, confirming, among other things, that the proposed program: does not conflict with other previously approved special uses of the Harbor; unreasonably impact regular



Raft up events allow organizations to tie vessels to one another, for socializing while using the public anchorage. Permit conditions for raft-up events include: total number of allowable vessels, permissible times for use of generators, amplified music, and safety related terms.

activities on the bay; or impose on the neighboring residents. Following the review of application materials and planned activities, specific conditions are incorporated into the permit as part of the approval process. These conditions provide guidance for issues such as: use of amplified music, locations, set up requirements, etc. On the day of the scheduled events, Harbor Service Workers will check with event organizers to ensure the terms and conditions set for the event to be successful are being met.

The following steps demonstrate how the Harbor Department, Special Event Permit – Simple 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 burden factors for the staff that are responsible for performing this task within Harbor Department. 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		Burdened Factors		Total Burdened Rate
	Hourly Rate		Hourly Rate		
Harbor Services Worker	\$29.85	+	\$34.14	=	\$63.99
Harbormaster	\$114.53	+	\$131.00	=	\$245.53
Department Assistant	\$35.99	+	\$41.17	=	\$77.16

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.¹
 - d) Travel expenses incurred specifically to carry out the operation.

Using the personnel identified in Table 1, the direct costs for the Special Event Permit – Simple fee are found on line 1.1 (total salary and benefits on an hourly basis) in Table 1a below.

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

Table 1a

Fully Burdened Hourly Rates	Harbor Services Worker	Harbormaster	Department Assistant
Annual Salary & Benefits:	\$ 51,426	\$ 197,306	\$ 62,000
1. Calculate hourly salary & benefits			
1.1 Divide annual cost by direct hours available (1723)	\$29.85	\$114.53	\$35.99
Total Salary and Benefits	\$29.85	\$114.53	\$35.99
2. Indirect Overhead			
2.1 Compensated Absences 13.4% (<i>vacation, sick leave</i>)	\$4.01	\$15.35	\$4.83
2.2 General Administration 14.7% (<i>supervision, support services</i>)	\$4.39	\$16.84	\$5.29
2.3 Operating Expense 32.7% (<i>training, supplies, maint & repair</i>)	\$9.75	\$37.41	\$11.76
2.4 Citywide Overhead 53.6% (<i>Finance, City Manager, Human Resources</i>)	\$16.00	\$61.40	\$19.29
Total Indirect Overhead 114.4%	\$34.15	\$131.00	\$41.17
Total Burdened Rate:	\$64.00	\$245.54	\$77.16

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 Harbor Department, 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 14.7% of Harbor Department’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 32.7% for Harbor Department 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 Harbor Department 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 53.6% for Harbor Department is calculated by comparing the total cost of Harbor Department’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

	Time Estimate
Harbor Services Worker	20 minutes
Harbormaster	15 minutes
Department Assistant	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
Harbor Services Worker	20.00		0.33		\$63.99		\$21.33
Harbormaster	15.00	➡	0.25	X	\$245.53	=	\$61.38
Department Assistant	10.00		0.17		\$77.16		\$12.86
							\$95.57
					Proposed Fee		\$95.00

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.