

**SEATTLE CHILDREN'S RESEARCH INSTITUTE  
OPERATING POLICIES / PROCEDURES**

<b>DEPARTMENT:</b>	Research Institute Administration
<b>POLICY NUMBER:</b>	RIA-902
<b>REPLACES:</b>	New Policy
<b>EFFECTIVE DATE:</b>	July 1, 2009
<b>REVISION DATE:</b>	NA
<b>POSTED FROM:</b>	May 6, 2009 – June 6, 2009

**TITLE:** Core Rate Setting

**SUMMARY:**

Cores are required to review and establish rates on an annual basis. Rates must be based on actual costs and good faith estimates of expected usage. Rates in the initial year of a Core should be established in conjunction with the business plan that must be created and submitted to CDAC as per RIA-901. In fact, the Rate Schedule will be a key component of the Core business plan.

In subsequent years, rates must be reviewed and calculated on an annual basis. Each year's rates should be established based on a review of the prior year's financials, good faith estimates of any expected cost component and/or usages changes, and adjustment for any accumulated deficits or surpluses. The policies and procedures documented here define how this is to be done.

**BACKGROUND**

The following are some key regulatory restrictions that apply to rate setting in a Core:

- The Core must operate as a "closed, self-adjusting system": all allowable expenses and revenue related to the operation of the Core must be recorded in the Core's accounts; and all accumulated surpluses or deficits must be fed back into the charged rates to maintain the Core's fund balance within a limited range.
- When Core charges are applied to a Federal grant – i.e., when the Federal Government is the ultimate "customer" of the Core – the rates charged must be based on actual costs and set to recover no more than the actual cost of providing the service.
- Like most customers, the Federal Government is always happy to receive a price break. Core rates charged to the Federal Government may not exceed those

calculated from actual cost and usage projections, but they may be less than cost-based rates.

- Core rates when charged to the Federal Government must include only those charges allowable under applicable regulation. Steps must be taken to ensure that unallowable costs are excluded from the rates charged to the Federal government.
- The procedures resulting in Core rates must ensure that all costs are accounted for and accounted for only once. Costs that are included in the Core rates cannot be recovered elsewhere as well. So, for example, the rate charged to the Federal Government cannot include the depreciation on a piece of equipment purchased on a Federal grant.
- The rates charged to the Federal Government cannot underwrite those charged to anyone else. The connections, moreover, are not always obvious. Rates must be conscientiously calculated to avoid government subsidies, and the conscientiously charged for the same reason.
- Finally, rates and rate calculations must be simple. The government wants rates that facilitate audit and analysis. Rate schedules with myriad services offered to myriad user types based on complex calculations and obtuse cost analysis are to be avoided.

This policy has been created in response to these constraints and establishes the principles and procedures for establishing Core rates at the Research Institute in order to ensure our ongoing compliance with the applicable regulations.

Please note that this policy is augmented by two additional policies regarding Cores:

RIA-901: Core Creation

RIA-903: Core Operations

These policies, plus any policies governing the specific Core in question, should be reviewed prior to creating a rate proposal for the Core.

#### **POLICY/PROCEDURE:**

Research Cores administered by and through the Seattle Children's Research Institute are required to adhere to the following principles with regard to the calculation and charging of Core rates.

- 902-1 The basic rate calculation for a given good/service provided by a Core is determined by the following equation:

$$\text{Rate for Good/Service} = \frac{\text{Total Cost of Providing Good/Service}}{\text{Annual Usage of Good/Service}}$$

902-2 Step 1, then, is to define the goods or services the Core will provide. For example:

902-2.1 “Minute per Machine” or “Hour per Machine” for a Core providing self-service access to scientific equipment;

902-2.2 “Hour of Staff Time” for a Core providing individual expertise and technical support;

902-2.3 “Cage per Day” or “Creature per Day” for vivarium services;

902-2.4 “Per Test” for a Core providing testing services;

902-2.5 “Per Widget” or “Per Box/Case/Gross of Widgets” for a Core manufacturing widgets.

902-3 In defining a Core’s sales unit, it can be useful to consider the needs of your customers vis-à-vis their obligations to track and manage expenditures. For those customers charging your services to their federal grants, it will be necessary for them to link the cost of your unit to the benefit accrued to a given project. Smaller, more precisely defined units may be preferable in this case to larger, grouped units. So, for example, if your “widget” is such that a single project will require just one (1) widget, from a Federal costing perspective it would be preferable for your Core to charge for those widgets on an individual basis rather than by the box or case.

902-4 If the Core will provide more than a single good or service, it will be necessary to calculate the cost for providing each good or service separately. The cost of the resources used in the Core will need to be allocated across the various goods and services produced in accordance with the contribution the service makes to the end product.

902-4.1 For example: A Core provides testing services – “Test A” and “Test B” -- and employs two technicians. The first technician spends all her time conducting only Test A services; the second technician spends half his time conducting Test A services and half conducting Test B services. In calculating the cost to provide Test A, 100% of the first technician’s salary would be include along with 50% of the second technician’s. The cost to provide Test B would include none of the first technician’s salary, and half of the second’s.

902-5 Once the unit is defined, the costs of providing those units can be calculated and will typically include the following:

902-5.1 Labor Costs – Salary and benefits for the individuals whose labor is involved in producing the good/service and/or administering the Core.

- 902-5.1.1 Salary and benefits should be calculated based on the percentage of FTE that each individual spends working on the Core. For example, if an employee spends 50% of his/her time on Core activities, 50% of his/her salary and benefits should be incorporated into the cost calculation for the Core.
- 902-5.1.2 Include any projected salary increases or fringe benefit rate changes anticipated for the coming year in your calculation of labor costs. Be sure to account for the timing of the expected raise. So, for example, for an employee is expected to receive a 3% raise halfway through the year, you would calculate the associated labor cost at 101.5% of current salary (i.e., half a year at current salary + half a year at 103% of current salary).
- 902-5.1.3 Include the labor costs for all employees providing support to the Core in proportion to their Core-related work. Include administrative support (provided the costs of that support are not covered elsewhere).
- 902-5.1.4 As described in Section 4 above, if an employee's effort supports more than one product of the Core, the cost of that employee's labor should be distributed across the various products in accordance with the proportion of effort spent working on each.
- 902-5.2 Equipment – Subject to the following considerations, if the goods/services provided by the Core involve the use of capital equipment, the depreciation costs of the required equipment should be included in the rate calculations.
- 902-5.2.1 If the equipment was purchased by a Federal award, depreciation for the equipment should be excluded from the rate charged to Federal users. Depreciation in such cases may be charged to external users.
- 902-5.2.2 As described in Section 4 above, the Core provides more than one good/service, the depreciation costs for the equipment should be allocated across only those goods/services that result from usage of the equipment and in proportion to their usage time spent on each.
- 902-5.3 Supplies and Other Consumables – The cost of any supplies or other consumable materials used in the production of the Core's goods/services should be included in the rate calculations in proportion to their use by the Core.

902-5.4 Space and Facilities – If a Core utilizes dedicated space, and the cost of that space is not otherwise recovered through application of the Research Institute’s negotiated F&A rate, the cost of that space should be accounted for in the rate calculations. Contact the Director of the Office of Research Finance for information about the appropriate recovery of space costs.

902-5.5 Other Costs – Any other expenses incurred in the operation of the Core should be accounted for in the rate calculations in proportion to their use by the Core.

902-5.6 Overhead – Overhead is applied to a Core’s rates as follows:

902-5.6.1 Internal Customers -- Core charges will be charged to internal activities on a line that is subject to the Research Institute’s F&A rate. Accordingly, costs covered through the application of F&A should not be included in the internal rates charged by the Core.

902-5.6.2 External Customers – Because an external customer will not be charging Core usage to a Children’s activity number, F&A should be added to the external rates. This will ensure that the Core recovers the necessary facilities and administration costs involved in the external user’s usage of the Core.

902-5.6.3 In cases where the Core includes administrative costs not recovered through the application of F&A, such administrative costs should be included in the rates applied to all customers. It is, however, essential that costs not be duplicated. If any question of a costs inclusion in the F&A rate exists, the Director of the Office of Research Finance should be consulted for a clear determination of whether or not that cost can be included in the Core rates.

902-6 For Cores that have been running for one year or more, the final step in determining the cost of providing the goods/services is to account for any deficits or surpluses that have accumulated in the prior year. Because the Core represents a “closed system,” surpluses or deficits generated in the prior year must be incorporated into the calculation of the new year’s rates.

902-6.1 The amount of any accumulated deficit should be added to the cost of providing the good/service in the coming year. This will increase the per unit costs across the expected usage such that at the end of the projected year, the deficit is eliminated.

- 902-6.2 The amount of any accumulated surplus should be subtracted from the cost of providing the good/service in the coming year. This will lower the per unit costs across the expected usage such that at the end of the projected year, the surplus is eliminated.
- 902-7 Following calculation of the expected costs that will be incurred in producing the Core's goods/services, the next step is to estimate the expected usage for the coming year of the identified goods/services.
- 902-7.1 Usage should be separately estimated for each good/service that will have its own rate.
- 902-7.2 Usage should be calculated in units (e.g., hourly, daily, per visit, etc.) that are reasonable for the type of service provided. (See 902-3 for additional information on setting units.)
- 902-7.3 All usage must be tracked and incorporated in to the rate calculations, even if the good/service is provided without charge. Failure to include unpaid usage opens the door to compliance risks. (See 902-10 for more information on subsidies and uncharged usage.)
- 902-7.3.1 Consider a simple example: The Core providing a given service calculates the cost of providing the service to be \$1,000, and the estimated paid usage at 10 sessions. The rate per session is therefore calculated at \$100. However, the Center managing the Core has agreed to give two faculty members one free session each. Thus, total usage is actually 12 and the real cost per session \$83. Customers charged \$100 are therefore being overcharged by \$17, a potential audit violation when the customer is the Federal Government or someone using federal funds to pay for the service.
- 902-7.4 Usage estimates can be based on prior year actual, or calculations of total available units, with downward adjustments for downtime and other intervening factors.
- 902-7.4.1 Total available hours for 1 FTE in a year is 2,080, but adjustments should be made for downtime, PTO and other leave.
- 902-8 Once units, cost to provide the good/service, and expected units are known, the rate can be calculated using the equation provided in 902-1.

- 902-9 The calculations described above will result in actual cost rates for the Core's provided goods/services. Following describe the circumstances under which rates may be established at something other than actual cost for usage.
- 902-9.1 Except as described in Section 902-9.2, actual cost rates should be charged to the following users of the Core:
- 902-9.1.1 Internal users (i.e., those who will charge the Core's services to activity numbers or accounting units in Children's Lawson system).
- 902-9.2 In cases where the actual cost rate calculated as per the above exceeds the market for the good/service and, thus, is unlikely to result in utilization of the Core, it is permissible to establish rates for the Core charged to internal customers and, if desired, external customers **below** the calculated rate. However, when below cost rates are established it will be necessary to document plans for managing the deficits that will result from charging less than cost.
- 902-9.3 External customers of the Core may be charged whatever rate the market will bear. The amounts recovered in excess of the actual cost rates should be manage in accordance with the provisions of the policy on Core Operations, RIA-903.
- 902-9.4 "Incentivizing" rates – e.g., Center-member versus non-Center-member rates, after-hours rates, weekend rates, bulk rates, etc. – are to be avoided. As noted throughout the above, Core rates must be based in actual cost. Further, as described in Section 902-7.3, the usage estimates used in the rate calculations must include all usage, whether paid or unpaid, which makes rate incentives difficult to manage and a clear opening for audit violations. Any plans to offer such rates should be reviewed the Director of the Office of Research Finance and Chief of Research Operations (CRO), before an attempt is made to establish a rate schedule including them. Incentivized rates must be approved by the CRO and will only be permitted in one of two circumstances:
- 902-9.4.1 There is clear evidence that the rate differential is based in actual cost. So, for example, if the cost of providing a service between the hours of 6pm and 8am can be documented to be less than the cost of providing that same service between 8am and 6pm, it may be permitted to establish two rates – a daytime rate and an after-hours rate – for that service.

902-9.4.1.1 Recall, however, that per 902-4, any cost shared between the daytime service and after-hours service will need to be distributed between the two in accordance with the benefit each accrues from the cost.

902-9.4.2 The lower rate is to be subsidized by the Center, or other suitable source of funds, and such subsidies are documented in the Rate Schedule and managed in accordance with the requirements of RIA-903. In this situation, it is not the case that the Core is establishing multiple rates; rather, the Core (or the owner of the Core) is agreeing to share the cost of the service with a specified group of customers.

902-9.4.2.1 For example, imagine a Core with a calculated service rate of \$100 per session. The Center which operates the Core desires to give Center members a 25% discount on the Core services. In this case, it would not be permissible to simply charge Center members \$75 and “write off” the remaining \$25 as this would result in an overcharge to all other customers. Rather, the Center must establish procedures to ensure that the \$25 under recovery is charged to an appropriate discretionary fund so that the total rate charged remains at \$100.

902-10 There is no specified format for the Rate Schedule, though it must include the following sections:

902-10.1 Brief description of the goods/services sold by the Core.

902-10.2 Identification of the units sold by the Core.

902-10.3 Identification and calculation of the total cost to provide each type of unit. Explain any assumptions built into the cost calculations, including, but not limited to, the distribution of a cost across more than one sales unit. Provide enough detail for a financial assessment of your projections.

902-10.4 Identification of any prior year surpluses/deficits incorporated into the rates and calculations showing its impact.

902-10.5 Identification and documentation for the equipment used in the Core including acquisition date and cost, identification of the funding

- source that paid for the acquisition, and calculation of current depreciation.
- 902-10.6 Identification and calculation of the expected usage each unit. Explain any assumptions built into the usage estimates, and provide enough detail for a financial assessment of your projections.
- 902-10.7 Justification for any below cost rates included in the Rate Schedule.
- 902-10.8 Explanation of any rate incentives rates included in the Rate Schedule, including identification of the account that will cover any subsidies and the total estimated value of those subsidies.
- 902-10.9 Include any documentation supporting the projected rate(s).
- 902-11 For existing Cores, once the rate calculations are complete, they should be forwarded to the Director of Research Finance and the Chief of Research Operations for review.
- 902-11.1 The Rate Schedule will be reviewed and either approved or returned for explanation.
- 902-11.2 Once the Rate Schedule has been approved, the effective date will be determined and the approved rates charged accordingly (see RIA-903).
- 902-12 For new Cores, the completed rate calculations should be incorporated into the business plan described in RIA-902. The requirements of that policy should then be followed through to completion.

Submitting Office: Research Institute Administration

Approved by:

\s\ Erik M. Lausund, Vice President Research Operations, 7/1/09

\s\ James B. Hendricks, PhD 7/1/09  
President, Seattle Children's Research Institute