SSRC
Cost Allocation Methodology

Part I: The Double Step-Down Methodology

I. Cost Allocation Overview

SSRC applies a double step-down methodology in its cost allocation procedures. The proprietary software, MAXCARS, is the tool with which the step-down methodology is accomplished.

MAXCARS provides for the inputting of all allowable costs by cost center identifications consistent with the accounting code structure. This capability allows for efficient balancing with the financial reporting systems.

Additionally MAXCARS provides for the inputting of allocation statistics appropriate for the distribution of the identified indirect cost pools. Credits for direct billed payments, cost adjustments, and other valid and applicable costing factors are also facilitated within the software.

A. Initiating the Process

Determination of the data to be included within the cost allocation process is accomplished through:

1) application of OMB Circular A-87 guidelines,
2) interviews,
3) review of financial documents,
4) review of organizational structure, and
5) analysis of statistical data relative to benefit of services provided.
B. Establishing the Cost Pools to Be Allocated

Basically the organizational structure is analyzed to determine which departments or cost pools provide services to other departments. These cost pools become the “Central Service Departments” in the cost allocation plan.

Next each cost pool is evaluated to determine the activities or services provided. The costs are then broken into subparts or functions such that each activity can be allocated on a statistical measure that is relevant to the service provided and the benefit received.

Line items of expenditures are analyzed to determine which functions receive the benefit of the costs. Distributions of these costs are made according to the determined benefit of each function.

C. Establishing the Statistical Measurements or Bases for Allocation

Available statistical measurements are evaluated to establish the most equitable and meaningful basis for allocating each function within each Central Service Department. Consideration is given to determining the measurement that most appropriately demonstrates its relationship to the receiving units. For example a function that is driven by the number of employees within the benefiting departments can be allocated by number of employees. Similarly a function that is driven by the number of transactions for each benefiting department can be allocated by the number of transactions.

D. Accommodating Exceptions and Adjustments

Applicable cost adjustments for unallowable costs and for use charges are incorporated into the appropriate schedules. Credits for direct billings, special revenues, etc. are entered into the computation cycle.
II. The Double Step-Down Methodology

Because Central Service Departments provide services to other Central Service Departments, SSRC employs a double step-down procedure. Simply stated, this allows all Central Service Departments to allocate costs to all other Central Service Departments. Since the Central Service Departments cannot simultaneously allocate their costs, the process must be done sequentially, one department after another. The second step-down allows for the equitable allocation of the costs that the Central Service Departments receives from one another.

To demonstrate the potential inequity of a single step-down, consider the costs of a Purchasing function and an Accounts Payable function. Purchasing processes the purchase orders for the materials and supplies that Accounts Payable consumes. This cost is rightfully allocable to all the departments that Accounts Payable serves. If Purchasing allocates its costs after Accounts Payable allocates its costs, and then the costs that are attributable to the services provided to Accounts Payable will be prorated to the other departments served by Purchasing. This method can then send costs to departments disproportionate to the benefit received from those costs.

Comparably Accounts Payable provides services to Purchasing. Similarly if Accounts Payable allocates its costs after Purchasing allocates its costs, then the costs that are attributable to the services provided to Purchasing will be prorated to the other departments served by Accounts Payable. Again this method can send costs to departments disproportionate to the benefit received from those costs.

The double step-down is supported by the OMB A-87 consistency of allocation requirement and has for over twenty years been widely accepted by Federal Cognizant Agencies.

A. The First Step-Down

The rule for this first round of allocations is that each Central Service Department can allocate to any other department regardless of the sequence of the departments and can allocate to itself providing the statistical measurements indicate a basis for the allocations.

1. The Process

The process of allocating during this round is achieved sequentially consistent with the order of the Central Service Departments. As each Central Service Department performs its allocations it allocates:

1) costs from the audited financials,
2) cost adjustments,
3) credits, and
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2. The Results
At the completion of the first step-down each Central Service Department has the allocated costs from itself and from the Central Service Departments sequenced after itself. These costs will be allocated in the second step-down.

B. The Second Step-Down
The rule for this second round of allocations is that each Central Service Department can allocate only to any other department sequenced after the allocating department providing the statistical measurements indicate a basis for the allocations.

1. The Process
The process of allocating during this round is achieved sequentially consistent with the order of the Central Service Departments. As each Central Service Department performs its allocations it allocates:

1) costs received from other Central Service Departments that have completed their second round allocations, and
2) costs received in the first round from itself and from the Central Service Departments sequenced after the allocating department.

2. The Results
At the completion of the second step-down each Central Service Department has completed all allocations. All Central Service Departments have been cleared of all costs. The costs have either been adjusted out of the cycle or sent to Receiving Departments based on equitable allocation statistics.

C. Supplemental Comments
When the relationships between and among the Central Service Departments is greatly intertwined, it may be prudent to implement three or more step-downs. Most often the double step-down is sufficient to accomplish an equitable allocation of all costs.

If more than two step-downs are required the rules for all rounds of allocation except the final round are the same as defined above for the first step-down. The final round always follows the rules as defined above for the second step-down.