

State of Nevada
Department of Administration
Division of Internal Audits

Audit Report

**Administrative Services Division
Building Depreciation
Nevada System of Higher Education**

Report No. 11-05
June 2011

EXECUTIVE SUMMARY
Division of Administrative Services
Depreciation of Nevada System of Higher Education
Buildings and Improvements

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**Objective: Can the State Increase Revenues by Recovering Depreciation
from the Nevada System of Higher Education?**

**Evaluate Recovering Building Depreciation Expenses
from the Nevada System of Higher Education..... page 4**

The State can increase revenues by about \$16 million annually by recovering building and improvement depreciation expenses from the Nevada System of Higher Education (NSHE). We reviewed over \$1.3 billion worth of NSHE buildings and improvements funded by the State. Our review revealed the State does not recover depreciation from NSHE for these projects. Federal guidelines allow the State to recover depreciation expenses for the use of buildings and improvements constructed with State funds. When an NSHE entity fully supported by the General Fund occupies a building financed by the General Fund, there is no benefit to the State for recovering depreciation. However, when an NSHE entity receives non-General Fund revenues and occupies a building financed by the General Fund, NSHE could pay building depreciation expenses. We surveyed two-thirds of the states and found that none were collecting building depreciation from their university systems; however, several are reportedly considering whether or not to collect building depreciation in the future.

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Timetable for Implementing Audit Recommendation

INTRODUCTION

At the request of the Executive Branch Audit Committee, we conducted an audit of building depreciation¹ expenses the State may recover from the Nevada System of Higher Education (NSHE). Our audit focused on whether the Department of Administration, Administrative Services Division (Division) could increase the State General Fund by recovering depreciation for State-funded buildings used by NSHE.

Division's Role and Public Purpose

The Division was created within the Department of Administration in 1993.² The Division provides accounting services to the Department's divisions and other agencies, such as the State Public Works Board. In total, the Division supports 98 department and agency budgets. Additionally, the Division is responsible for preparing the statewide allocation of administrative costs, such as budgeting, State library services, and depreciation expenses.

The Division has 21 staff and a budget of almost \$2 million for fiscal year 2008. The Division is funded by charging fees for the services it provides.

NSHE's Role and Public Purpose

NSHE is governed by an elected Board of Regents. The Board of Regent's vision includes advancing student learning to the highest level and expanding knowledge through teaching and research. There are 8 institutions within NSHE.³ Approximately 42 percent of NSHE's almost \$1.4 billion fiscal year 2007 revenues were State General Fund appropriations. See Exhibit I.

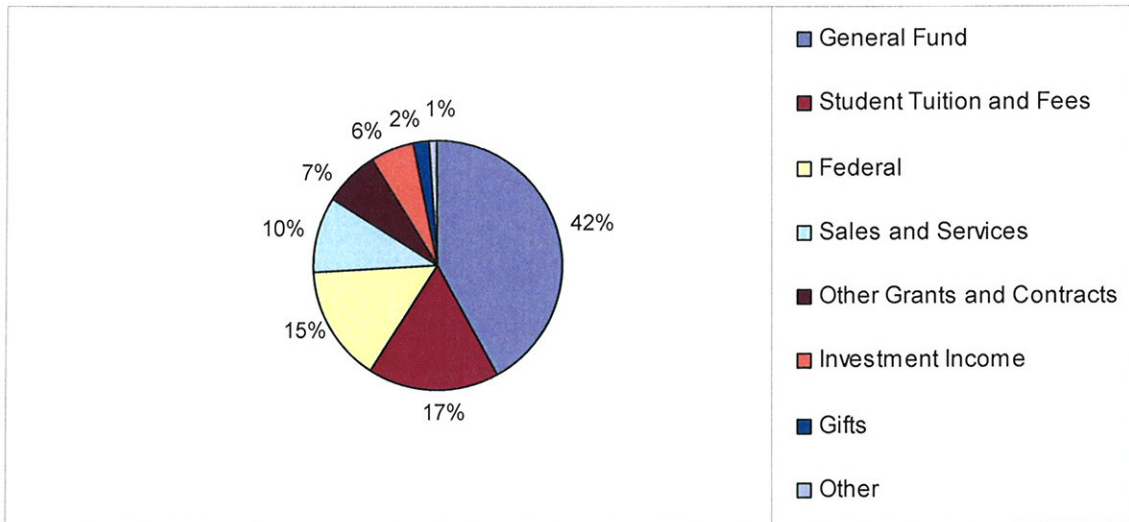
¹ Depreciation is an annual charge for the loss in value to a building because of wear and tear, deterioration, or obsolescence over its useful life.

² Nevada Revised Statutes 232.213, 232.2195.

³ NSHE consists of the following institutions: College of Southern Nevada; Great Basin College; Desert Research Institute; Nevada State College; Truckee Meadows Community College; University of Nevada, Las Vegas; University of Nevada, Reno; and Western Nevada College.

Exhibit I

2007 NSHE Revenues by Percentage



Source: NSHE

Scope and Objective

We began the audit work in March 2008. In the course of our audit, we reviewed NSHE's building and improvement depreciation expenses. We reviewed federal regulations for charging depreciation. For the period 1967 through 2007, we reviewed Nevada State Legislature appropriations and authorizations bills and Legislative Appropriations Reports. We reviewed the State Public Works Board's Recommended Capital Improvement Program for each biennium beginning with 1967. We also reviewed NSHE data. We determined, to the extent possible, the amount of State funding for the construction of buildings or improvements used by NSHE.

We used appropriations and authorizations by the Nevada State Legislature as the basis for determining the amount of State General Fund monies used to construct NSHE buildings and improvements. We used this amount to determine depreciation. We excluded buildings and improvements older than 40 years, the limit to which depreciation expenses can be charged and recovered.⁴ We concluded field work and testing in September 2008.

⁴ The State Controller determines how buildings and improvements are depreciated. Buildings, and improvements to buildings, are depreciated over 40 years. Improvements to property other than buildings are depreciated over a 20-year period, such as parking lots and lighting, fencing, and irrigation systems.

Our audit focused on the following objective:

- ✓ Can the State increase revenues by recovering depreciation from the Nevada System of Higher Education?

The Division of Internal Audits expresses appreciation to the management and staff of the Department of Administration, Administrative Services Division; Office of the State Controller; State Public Works Board; and the Office of the Vice Chancellor for Finance for their cooperation and assistance throughout the audit.

Contributors to this report included:

Warren Lowman
Executive Branch Auditor

Paul Chalekian, Ph.D.
Executive Branch Auditor

Division of Administrative Services Response and Implementation Plans

We provided draft copies of this report to the Division's Administrator and Nevada System of Higher Education officials for review and comment. Their comments have been considered in the preparation of this report. The Divisions comments are included in Appendix A. In its response, the Division accepted the recommendation we made. Appendix B includes the Division's timetable to implement our recommendation.

NRS 353A.090 specifies that within six months after the Executive Branch Audit Committee releases the final audit report, the Chief of the Division of Internal Audits shall evaluate the steps the Administrative Services Division has taken to implement the recommendations and shall determine whether the steps are achieving the desired results. The Chief shall report the six-month follow-up results to the Committee and Division officials.

The following report contains our findings, conclusions, and recommendations.

Can the State Increase Revenues by Recovering Depreciation from the Nevada System of Higher Education?

The State can increase revenues by recovering building and improvement depreciation expenses from the Nevada System of Higher Education (NSHE). We estimate the State can recover almost \$16 million annually or \$415 million over the remaining useful life of the buildings and improvements. However, we found no other states currently recovering building depreciation from their university system.

Evaluate Recovering \$415 Million in Building Depreciation

We reviewed over \$1.3 billion worth of NSHE buildings and improvements funded by the State between the years 1967 – 2007. Our review revealed the State does not recover building and improvement depreciation from NSHE for these projects.

Federal guidelines allow the State to recover depreciation expenses for the use of buildings and improvements constructed with State funds.⁵ When an agency fully supported by the General Fund occupies a building financed by the General Fund, there is no benefit to the State for recovering depreciation. In this situation, the General Fund would be reimbursing the General Fund. However, when an agency receives non-General Fund revenues and occupies a building financed by the General Fund, the State could recover building depreciation expenses.

We reviewed 37 years worth of NSHE budget data and its 2006 – 2007 annual financial report. Based on this review, about 51 percent of NSHE's revenues were non-General Fund. As such, we estimate the State can recover depreciation from NSHE's non-General Fund revenues of almost \$16 million annually. See Exhibit II.

⁵ The Office of Management and Budget (OMB), Office of Federal Financial Management represents the State could charge NSHE for building depreciation pursuant to Office of Management and Budget (OMB), 2 CFR Part 225 – *Cost Principles for State, Local, and Indian Tribal Governments* (OMB Circular A-87), August 31, 2005. NSHE should use the provisions outlined in OMB, 2 CFR, Part 220 – *Cost Principles for Educational Institutions* (OMB Circular A-21) to calculate the amount of building depreciation.

Exhibit II

Estimated Depreciation Expenses the State May Recover from Buildings and Improvements Financed by the General Fund

	Annual Depreciation Charges	Recoverable Annual Depreciation (51%)
Buildings & Improvements Funded Between 1967-2005	\$18,945,000	\$ 9,662,000
Pending Buildings & Improvements Funded Between 2003-2005	\$ 9,365,000	\$ 4,776,000
Buildings & Improvements Approved by 2007 Legislature	\$ 2,965,000	\$ 1,512,000
Total	\$31,275,000	\$15,950,000
Estimated recoverable depreciation over the buildings and improvements average remaining life span (approximately 26 years) is \$415 million.		

Pursuant to federal guidelines, all agencies need to be charged depreciation equitably. Consequently, some agencies may require additional resources or reduce costs to pay depreciation expenses.

We surveyed two-thirds of the states and found that none were collecting building depreciation from their university systems. One state, Virginia, charged, collected and then returned depreciation expenses to its university system. Several states are reportedly considering whether or not to collect building depreciation in the future.

NSHE Areas of Concern

NSHE has two main areas of concern regarding payment of depreciation to the State: building ownership and cost allocation.

Building ownership – NSHE represents it, not the State, owns the buildings. When a building, which is wholly or partially paid for by the General Fund, is completed, the State Public Works Board turns over control of the building to NSHE. Likewise, other State buildings (non-NSHE buildings) funded by the General Fund are turned over to the control of State Lands. Buildings owned by State Lands are depreciated and charges recovered through the Statewide Cost Allocation Plan (SWCAP).

Cost allocation – NSHE does not believe it is subject to building depreciation expenses charged through the SWCAP.

Recommendation

1. Evaluate recovering depreciation expenses from NSHE.

Appendix A

Administrative Services Division Response and Implementation Plan

JIM GIBBONS
Governor

STATE OF NEVADA

ANDREW CLINGER
Director



EVAN DALE
Administrator

DEPARTMENT OF ADMINISTRATION
ADMINISTRATIVE SERVICES DIVISION

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Carson City, Nevada 89701-4204
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September 18, 2009

TO: William Chisel, CPA, Chief, Division of Internal Audit
FROM: Evan Dale
SUBJECT: NSHE Building Depreciation Audit Status Report

1. **Recommendation:** Evaluate recovering depreciation expenses from NSHE.

The Division of Administrative Services is in the process of determining building depreciation charges for State agencies that will be included in the fiscal year 2011 statewide cost allocation plan. Upon completion of this process, the Division will evaluate charging the Nevada System of Higher Education building depreciation.

Appendix B

Timetable for Implementing Audit Recommendation

In consultation with the Division, the Division of Internal Audits categorized the recommendation contained within this report as taking more than six months to implement. The Division should begin taking steps to implement the recommendation as soon as possible. The Division's target completion date is incorporated from Appendix A.

<u>Recommendation</u>	<u>Time Frame</u>
1. Evaluate recovering depreciation expenses from NSHE.	July 2012

The Division of Internal Audits shall evaluate the action taken by the Administrative Services Division concerning the report recommendation within six months from the issuance of this report. The Division of Internal Audits must report the results of its evaluation to the Committee and the Division.

Our audit focused on the following objective:

- ✓ Can the State increase revenues by recovering depreciation from the Nevada System of Higher Education?

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Appendix A

Administrative Services Division Response and Implementation Plan

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