DEBUNKING INTERNAL SERVICE FUNDS: IMPROVING BILLING METHODOLOGY AND TRANSPARENCY TO THEIR CUSTOMERS

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Executive Summary

Across California and the rest of the United States, a disconnect exists between governmental operations and the accounting that supports them. Resonating from this disconnection, program managers experience inescapable administrative charges that hit a program's budget, which lack transparency and detail. Those costs that hit governmental programs are, in part, derived from internal service funds (ISFs). ISFs are governmental entities that operate as quasi-businesses, which provide goods and services to other governmental entities. Instead of seeking profit, ISFs operate on a cost recovery model that charges other governmental entities for their goods and services to break even. The accounting practices behind ISFs often leave their governmental customers confused by vague charges, feeling taken advantage of, and helpless to control their impact on their budgets.

This paper begins with background information on internal service funds and highlights some examples of problematic ISFs. A literature review section follows that summarizes academic discussion about significant ISF topics. To address issues with the billing methodologies and transparency concerns, this policy report then recommends implementing a revised Lewin's 3-step model for underperforming internal service funds to improve overall operations and customer comprehension of charges. This paper utilizes Lewin's 3-step model since it stresses communication as a fundamental approach to executing change in an organization while minimizing disarray. The emphasis on communication aligns with the need to repair and progress good relations with their customers. To more accurately apply this method to internal service funds, this paper recommends inserting an additional step called "Hold and Update" into Lewin's model to accommodate a more customized tactic to implementing change. After exploring various considerations when implementing change in ISFs, this paper outlines

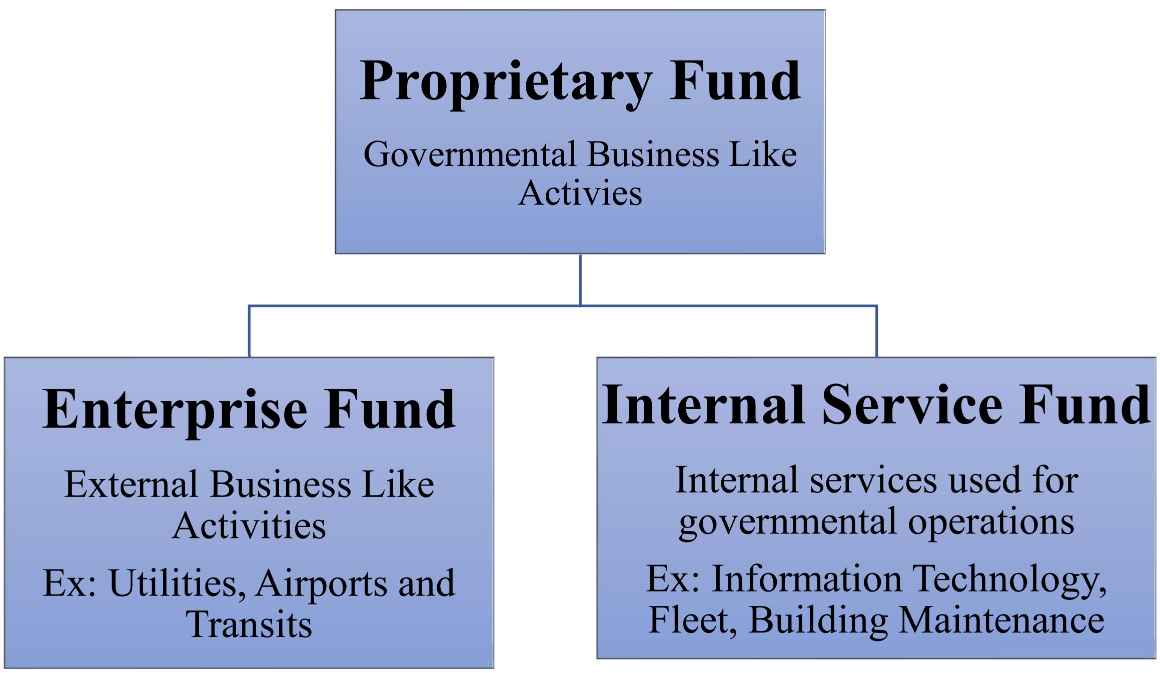
recommendations embedded in the revised 4-step model to improve billing methodologies and transparency. These changes aim to guide internal service funds to practice defensible accounting and to promote clarity to customers, enabling them to make more informed decision-making in their budget development and cost control.

Section I: Introduction

Understanding costs and maintaining governmental fund stability has become increasingly critical in this current period of economic uncertainty, where program managers are seeking to stretch every dollar possible to maximize the public good. Internal service funds deliver the backbone services for other governmental operations to function. From information technology, employee benefits, fleet management to building maintenance, ISFs provide an array of services that customers consider as overhead. Internal service funds provide these services across the entire government organization as distinct departmental and accounting entities. To pay for these services, ISFs treat other governmental departments as customers and package expenses to bill them for the services they use. Unfortunately, customers tend to know very little about the total bill that they receive for services, which often seem detached from their operations. ISFs may use convoluted or inconsistent billing methodology to pass their costs to the customers and/or fail to provide clarity to their customers about their billings.

The State of Vermont describes an internal service fund as a "fund created by governments to allocate the cost of certain shared activities while facilitating the use of multiple funding sources" (2019). As defined by the Governmental Accounting Standards Board (GASB) in Statement No. 34, an ISF is utilized to "report any activity that provides goods or services to other funds, departments, or agencies of the primary government and its component units, or to other governments, on a cost-reimbursement basis" (1999, para. 68). An internal service fund may be considered a proprietary fund, which is used as a blanket term that describes governmental funds that perform specific business-like activities. Enterprise funds and internal service funds fall under the proprietary fund category. While an internal service fund focuses on services for governmental operations, an enterprise fund provides external services, such as a water utility enterprise fund, to rate-paying customers. ISFs have more flexibility in terms of funding sources and usage of funds, while enterprise funds restrict the revenue the fund collects to fund specific operations. For example, when a customer pays their water bill, the money is restricted to be only used to fund costs that ultimately provide water to the customer. Fewer restrictions, if any, apply to ISF collections as compared to an enterprise fund. Fewer restrictions on how money can be spent can lead to more creative usage of customer payments. When combined with transparency issues, ISFs can elude accountability with the funds they collect from their customers, which can cause customers to question what happens with their money.

Figure 1: Relationship between Proprietary, Enterprise, and Internal Service Funds



Billing methodology plays a pivotal role in internal service funds. Billing methodology describes the process in which an ISF allocates its pooled costs to customers. When a water utility enterprise fund determines how to bill its customers, the amount of water a customer uses provides a common element when determining how much a customer should pay. ISF must produce a cost allocation methodology that bills its customers accurately. For example, an information technology ISF may bill departments based on the number of users who possess a computer that can access the organization's network. The methodology seems like a good place to start, but what happens to a department that faces significant turnover and has vacant positions for long periods? Do departments that have many unused computers sitting in a vacant supply closet rack up charges, or should the customer receive credit for underutilization in their billings? If a department employs many positions that do not require their own computer, but share a common computer to enter their timesheet data, does the department only get billed for one computer, despite many employees needing to access it? Questions and scenarios like these plague ISF methodologies, and the amount that is billed to a customer may be mired by numerous one-off adjustments that are not evenly applied across all customers.

A 2012 Utah State Legislature internal service fund oversight report described some of their internal service funds' billing processes as "cumbersome, lengthy, and difficult to resolve issues, " and stressed that their billing would be dependent on the person spoken to. Additionally, the report highlighted that there was overwhelming support for the need for customer agencies to approve payment of ISF invoices before payment is transferred, since prior customer approval was not required. Establishing an accurate billing methodology that considers scenarios such as these is essential to the accountability of an ISF.

Another important aspect to emphasize regarding internal service funds and accounting in general is that management is ultimately responsible for the financial condition of their operations and the accuracy of the financial statements, even if they lack a clear understanding of accounting concepts like debits and credits. In 2022, there were approximately 190,000 open accounting positions in the United States, creating a severe accounting shortage (Garima, 2025). This shortage continues. One must not assume that faults with billing methodology and subsequent accounting belong solely to fiscal staff. Financial statements must be signed by management, who acknowledges their responsibility for the accuracy of the numbers presented. Accounting affects the core of operations in business. All employees engage in financial transactions and must demonstrate a commitment to encourage accuracy. All program managers must be aware and gain an understanding of their charges to draw attention to possible concerns to assist with proper financial reporting. Therefore, ISFs must not only improve their operations but also provide customers with fair and accurate charges that are presented, allowing any discrepancies to be easily identified. It is important to state that all members of an organization participate in accurate financials and must assume responsibility for oversights and not just accounting personnel.

Examples of Internal Service Funds Issues

The policy report aims to draw attention to internal services funds and their financial impact on government entities by emphasizing that ISFs create and perpetuate unreasonable billing methodologies and operate under obscure and confusing conditions. By employing a revised Lewin's model to facilitate organizational change, ISFs can apply the defensible billing methodologies and transparency recommendations outlined in this paper that incorporate various considerations, such as equity and feasibility, to improve customer communication and cost allocation. Due to limited or non-existent statewide or nationwide studies of internal service funds, statistical information and findings remain an understudied topic. Anecdotal case-by-case analysis is the only means to depict current issues with ISFs. This section exemplifies two recent published audit analyses of ISFs and their struggles with proper accounting and/or clarity with stakeholders.

In 2020, KPMG, one of the "Big Four" accounting firms, was hired to analyze the County of Santa Barbara's internal service funds. Through interviews and survey analysis, KPMG staff documented that the county departments had little understanding of the cost allocation process to set rates for customers, little documentation, and deficient reasoning as to what and why assumptions were made to determine current rates and poor communication between ISFs and customers during the budgeting process (County of Santa Barbara, 2020). Poor documentation to assist with duplicating calculations, inexperienced accountants, very manual data entry requirements, lack of budgeting software solution to preserve data and little customer outreach contributed to the poorly performing county ISFs. Problems stemming from these issues included over/under-collecting from customers, inconsistent billing allocations and the ISF being unable to defend their practices. Recommendations to assist the county with ISF operations were to increase staffing personnel with cost accounting experience, establish ISF monitoring processes to ensure full cost recovery and create training sessions with staff and customers to increase transparency.

In 2020, NBS, a local government consulting firm, was employed to analyze the County of Ventura's ISFs. From their overall analysis, the County of Ventura possessed a high degree of defensibility and proper documentation for cost allocation, cost accounting, and rate development (County of Ventura, 2020). The few recommendations that NBS provided were some specifics about rate calculations for the county’s ISFs, and guidance to improve documentation to enhance communication to customers and other stakeholders. Although the County of Ventura was much more successful when compared to the County of Santa Barbara, transparency represents a common element to emphasize in the operation of an internal service fund in addition to developing and maintaining a consistent and reasonable cost allocation.

Section II: Literature Review

While literature associated with internal service funds exists, an overarching and comprehensive look at internal service fund usage, comparison, and statical data set remain either largely undefined or is narrowed to a particular region. Among the literature, three topics stand out as common problems when discussing ISFs. This literature review examines how ISFs are often compared to external businesses, closely analyzed for their cost allocation methodologies, and subject to concerns about transparency.

A. Comparison to External Business

Internal service funds can easily be compared to external businesses because their accounting structure shares similarities to private sector accounting. ISFs utilize the full accrual method of accounting akin to what publicly traded companies use for their accounting. Full accrual accounting recognizes transactions when they impact an entity, regardless of when cash is exchanged. Most other governmental funds utilize the modified accrual basis of accounting that contains some key differences when recognizing transactions (Fiscal Management Division, n.d.). Therefore, the ISF accounting structure distances ISFs from other governmental divisions while also supporting similarities to external business operations. Also, ISFs serve other governmental divisions as customers similar to a business serving clients and both employ activity-based cost management systems (Cokins, 2015). Costing systems that identify the cost of each activity are called activity-based costing. Subsequently, an activity is an event or task with a specified purpose (Datar et al., 2018). The similar accounting structures and operational perspectives welcome academia to compare ISFs to external businesses.

Diving deeper, a key distinction in full accrual accounting requires the recognition of depreciation costs and long-term debt which differs in accounting practice compared to other modified accrual governmental funds. The recognition of these costs in accrual accounting can lead to more inflated upfront costs in the provision of goods and services and distort rates especially when the rates are charged to funds utilizing modified accrual (Falk & Granof, 1990). Due to how these costs influence ISF cost recovery, the usage of full accrual accounting and the need for experienced accountants to manage this accounting have triggered critical examination to transition away from ISFs and their accounting structure (Modlin, 2023). Academics highlight this distinction and the resulting complexities between ISFs and other governmental funds to question why ISFs provide these services instead of outsourcing them to external businesses. Why require specialized accountants who need to know another system of accounting? Therefore, just the certain unique accounting elements of ISFs evoke scrutiny that other governmental entities would not get otherwise.

Services and the quality of those services offered by ISFs compared to external companies invite additional criticism. Although other governmental services experience privatization, the ISFs seem heavily targeted because of their quasi-business-like structure that invites easier comparisons to external businesses providing similar services. For example, information technology internal service funds are more frequently considered for outsourcing in government operations than compared to other services, due to the widespread availability and standardization of IT solutions. Conversely, if a department is not forced to utilize ISFs, then ISFs provide an in-house alternative to external companies. Managers make more informed decision making with the availability of ISFs about whether it is cheaper to provide services in-house or seek services from external businesses (Swiss, 1991). Quotes requested from internal service funds are evaluated against quotes from external businesses and thus receive feedback and comparisons from their customers. This seems unfair when compared to other governmental organizations that offer exclusive services, such as protection services from sworn deputies, that no alternative exists. Although not entirely a negative note, the availability of competition forces ISFs to adapt to external pressures and increase productivity and efficiency through specializing in providing catered services to their governmental organization (Ukeles, 1982). ISFs can draw a comparative advantage when judged to external business because of their ties to the governmental organization and the institutional knowledge that comes with a close association.

B. Costs Allocation

Since internal service fund focus on cost recovery, cost allocation and by extension cost accounting captivate the discussion in the literature involving internal service funds. While ISFs can improve cost accounting and cost allocation within governmental organizations, they can also dramatically distort cost accounting if mishandled and permit interfund financial resource manipulation (Chang & Robert, 1991). Particularly troubling, fiscal management can find creative accounting practices that target certain governmental departments over other departments to their benefit. ISF resources could be redistributed to governmental funds through a variety of means. (Falk & Granof, 1990). An example would be allocating more information technology ISF costs to a particular customer like a sewer enterprise fund. If more IT costs are allocated to the sewer enterprise fund, then sewage rates paid by customers would have to increase. If the allocation is not justified, then IT costs are shifted away from other departments funded by general fund dollars to external customers paying for sewage. Therefore, general fund departments realize more savings at the expense of sewage rates. This example demonstrates how creative management manipulation can shift costs away from flexible general fund dollars to sewage enterprise funds with restricted dollars meant only to pay for costs associated with providing sewer services.

The number of customers and fund balance create concerns regarding the distribution of costs and financial stability of internal service funds. A limited customer base can create higher service costs for the receiving entities and cause ISFs to be unable to adequately recover their costs if trying to use traditional market mechanisms (Gianakis, 1995). Few customers challenge the necessity for ISFs in small governmental organizations. A large pool of customers enables ISFs to delicately spread their overhead costs among their customers lowering overall costs to the individual customer. Therefore, if high rates push existing customers to seek external services then remaining customers share a higher burden of overhead rates. Additionally, ISFs must consider fund balance surpluses and deficits and how they impact customer rates. Certain ISFs need to charge extra at times to accumulate a justifiable reserve for expected future catastrophe losses (Chang & Freeman, 1991). While building reserves for contingency is generally promoted, additional costs beyond cost recovery are pushed to the customers. Cycles of surplus and deficits, over- and under-collection impact costs to customers that can lead to significant swings in rates and cause confusion if not properly explained to customers.

C. Transparency Issues

Lack of transparency over billing practices and the interaction between internal service funds and other governmental funds allows for confusion over the accounting and the broader function of ISFs. With limited guidance to the creation of ISFs, there is no exact accounting standard that dictates what organizations needs to be an ISF or what specific services and scope an ISF can provide (Gianakis, 1995). Executive management in an organization ultimately decides what roles ISFs play in a governmental organization (Falk & Granof, 1990). Executive management may force other governmental divisions in an organization to utilize ISF services when that may not be in the best interest of a particular division (Davis, 1991). Additionally, out of ease with accounting software, ISFs typically can charge customers without prior approval. This high level of managerial discretion, combined with potentially forced customer participation where budget and costs collide, can foster internal tension between ISFs and their customers that leads to transparency issues and mistrust.

<u>Section III: Organizational Change Framework: Lewin's Change Model</u>

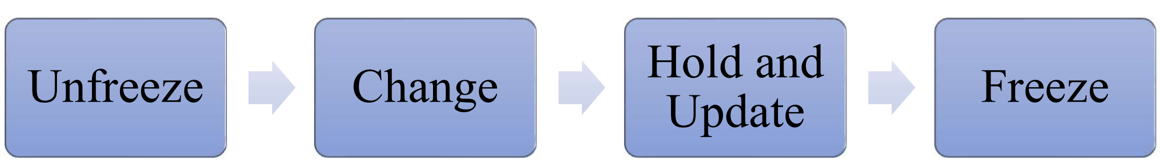
Lewin's (1947) 3-step change model serves as a foundational framework for implementing organizational change, and how it can be applied to internal service funds. Lewin's model consists of three steps: Unfreezing, Change, and Freeze (See figure 2). Due to the unique nature of the budgeting process of internal service funds, an additional step, "Hold and Update" will be inserted into the model (between steps two and three) to better conform to the budgeting timeline practiced by ISFs. This section expounds on each step of the revised model and how the model offers a comprehensive strategy to implement organizational change concerning internal service funds.

Figure 2: Lewin's 3-Step Change Model

Lewin's initial model addressed more of an emotional and performance-based approach to change regarding the tone and style of work within an organization rather than the organization itself (1947). Lewin's model has since been expanded and repackaged to describe broader organizational change, but keeping the basic principles of each step intact. A key feature of Lewin's 3-step model is that the model accommodates the rigidity of governmental organizations by emphasizing its intention to take a stable organization, quickly implement change, and then form a new solid structure. Utilizing this model reduces organizational chaos and discomfort for employees and other stakeholders by minimizing potential complexities during the transition (Awati 2022).

In specific regard to internal service funds, the budgeting process introduces a unique consideration. ISFs are expected to complete their budgets before other governmental funds to allow their customers a better understanding of their overhead costs before developing their programmatic expenses. Once the ISF budget is finalized, there exists a holding period before a governmental jurisdiction's budget is adopted and the fiscal year begins. This creates a distinct interval of time when an ISF's budget is completed but not yet implemented. This paper defines this period as the "Hold and Update" phase and inserts this step in between the second and third steps of Lewin's model to specifically address organizational change in internal service funds (see figure 3).

Figure 3: Revised Lewin's Model



Unfreezing an organization begins by building awareness of the need for change and introducing new ideas into the organization. Key activities to undertake during the Unfreezing step include: assessing current structures and processes to identify what change and why, clearly communicating the reasoning and benefits of the proposed changes to all stakeholders, engaging key stakeholders early to secure commitment and support, aligning the change with the organization's vision and mission and addressing employee concerns and fostering broad organizational support (Awati 2022). Major planning to prepare the organization must take place, and management must create an urgency among the employees (Malik 2022).

Disruption of the status quo embodies the Change step of Lewin's model. Using the planning in the Unfreeze phase, this step aims to dismantle the current processes to the proposed changes and align with the organization's desired direction in the least amount of time and as seamlessly as possible (Awati 2022). Heightened communication among stakeholders helps reduce the disorder during this step. From a timing perspective, implementing the change should take the least amount of time possible to minimize disruption to overall operations.

Due to when ISFs typically fall in the budgeting timeline, internal service funds must produce their budgets earlier than other government departments because customers need to know ISF costs in advance to accurately budget around them. Once an ISF completes its budgeting, cost allocations are fixed for the customers. However, since ISF cost allocations impact multiple customers, any change in costs and subsequent budgeting for an ISF means a corresponding adjustment in rates for all customers. Any change in ISF charges can cause major disruption across the governmental organization. Therefore, there exists a period when ISFs have their budgets completed and should not be changed, but the budget has not been adopted or implemented for the new budget year. This unique ISF period of time warrants its own step in

Lewin's model. Rather than freezing after implementing the change, the ISF waits in a holding pattern while customers budget around their ISF allocated costs. The Hold and Update period allows the ISF staff to answer any questions their customers ask and incorporate any operational updates that arise from the customers as long as it does not impact the cost allocation. Additionally, ISF staff can prepare any outstanding logistics to ensure a smooth transition to the services and rates the previous steps outlined.

The start of the budget year commences the Freeze step of the revised model. Organizational change should be fully implemented, stakeholders informed of the changes, and staff ready to maintain the new procedures. This final phase solidifies the change and ensures that the new standard is accepted and integrated within an internal service fund.

Section IV: Considerations

This section of the paper outlines what types of framing an internal service fund should consider when implementing change to existing billing methodologies and enhancing transparency with customers.

A. Equity

Internal service funds can provide services to their customers across their entire organization ranging from enormous departments with many employees to small divisions with only a few. Customers have specific and individualistic needs that an ISF must strive to meet while maintaining overall service to the entire organization. An ISF must carefully assign attention and resources equitably while navigating demands and diverse customers. The GFOA emphasizes that charges must be recognized as fair and legitimate to its customers when determining the basis of allocation (2013). Billable work versus non-billable work portrays a significant dilemma when ISF program management must determine priorities. Concentrating on completing billable work orders may be tempting for an ISF where persistent deficits and unrecoverable costs impose financial hardship. This conflicts with performing non-billable services whose costs have already been paid for by customers. Therefore, an ISF must formulate a written element into the cost allocation methodology that promotes equity and fairness to customers when determining how work orders rank in importance to one another.

Also, an ISF must be aware of the funding differences with their customers. Depending on the resources available to a customer, some services provided by an ISF may be handled internally by the customer. For example, a health and human services (HSS) department employs a few IT professionals to maintain their complex website, whereas IT maintains and updates all other customer websites. Since HSS provides services that IT provides for other departments, HSS should receive some sort of reduced rate for providing its own services. On the other hand, an ISF must devise a system where disparities in customers' resources prevent a particular customer from out-gaming the system. Website maintenance may absorb a larger portion of the IT's overhead charges than other IT services required by HHS and other customers. By simply providing this one service, HHS may avoid a large allocation of overhead for this particular service and instead push more overhead costs onto other customers. For customers with varying needs, internal service funds have to ensure rates reflect services used but still equitably share other costs.

B. Economics

When considering how internal service funds create a methodology, activity-based costing forms some sort of component on how to recognize and allocate costs in that methodology. An ISF needs to understand the cost drivers that encompass their expenses and how to accurately charge their customers without spending too many resources getting down to the penny. Administrative burdens to devise, maintain, and update the activity-based costing accounting, overengineering for small operations, and costly accounting systems and software can diminish the value brought by comprehensive methodologies. The law of diminishing returns describes this scenario by detailing that an increase in the factors of production, along with a fixed amount of other production factors, will result in the increases in output of product becoming smaller and smaller (Johnson, 2005). In the context of an ISF, a methodology with overly complex formulas that require many resources, i.e. labor hours, manual actions, and costly overhead expenses, then the value to distinguish costs from belonging to one customer than another may be too costly for the value it brings. Therefore, when determining whether a cost should be directly charged to a customer or absorbed into a core business expense, the economic costs to measure and allocate the costs to a particular customer must weigh into the ultimate methodology.

C. Feasibility

Implementing organizational change to an ISF utilizing the revised change model requires upfront work and ISF management must determine what is feasible to alter. Technology presents a limitation to the extent of how precise a reworked cost allocation and billing system can be when implementing feedback from customers. Additionally, accounting shortages exist across the nation. The number of accountants dropped 16% compared to figures since 2019 (Mezistrano, 2025). The continued exodus of accountants in the industry already places strain on maintaining existing accounting structures before attempting to implement new practices. The shortage of skilled accountants could cause management to weigh the value of implementing best practices versus realistic actuals.

D. Power Dynamics

Resistance to change is a natural response when implementing organizational change. 70% of change programs fail to achieve their goals in part due to employee resistance (Ewenstein et al., 2015). This paper examines resistance to change stemming from accounting personnel, customers, and ISF program managers.

Authoritative accounting bodies create numerous guidelines and regulations that control the flow of accounting. Additionally, accountants thrive on precedent because it signifies that another person has validated previous actions that have eventually gained acceptance as a practice. These guidelines and precedents form a powerful force that pushes accountants to stick with what they know. Although many accountants confront shifting tax laws every year, less dramatic and fewer in frequency changes in GASB regulations can disrupt governmental accountants further than more accustomed tax accountants. Whether existing accountants possess the skillset and adaptability to implement change must be factored into how ISF management shifts power dynamics and traditions.

ISFs can receive resistance to change from ISF customers as well when deviating from the status quo. Inherently, a poor cost allocation among customers produces winners and losers in the current methodology. A bigger department may be absorbing more than its fair share of ISF overhead charges than a small department, and vice versa. An ISF must consider how to navigate equity among existing customers regarding rates and combat issues to moderate resistance to change. A comparison of new and old rates and how to temporarily let their discrepancies impact new rates may help ease the transition to overcome resistance and gain trust.

Shifting power dynamics play an internal role in the power structure of an internal service fund as well. ISF mid-level managers can play an integral part behind the financials, not only in cost recovery, but also in the discretionary decisions that influence how services are priced and allocated. When an ISF lacks transparency, management discretion may impact whether or not a customer is charged for services, and if so, how much. However, at times, discretion may benefit the ISF and its customers due to the occurrence of unforeseen situations where existing procedures fall short. Since management may enjoy the level of informal power that comes with ultimately deciding if a customer receives favorable rates or waived charges, removing this level of autonomy presents a challenge to internal authority among management and adds a level of complexity to add enough flexibility to accommodate niche circumstances.

Section V: Recommendations

Utilizing the revised Lewin's model of the Unfreeze, Change, Hold, and Update, and Freeze process, an internal service fund should leverage the model's emphasis on communication to smoothly implement strategic updates to their organization and practices. This paper recommends reworking the billing methodology and increasing transparency among stakeholders as the central areas to improve with internal service funds. This recommendation outlines an improved billing methodology framework using the revised model while observing the considerations mentioned earlier. Additionally, all stages of the revised model must promote more communication with stakeholders to increase buy-in by providing clearly defined customer cost allocation methodology rates and productive channels to solicit feedback.

Billing methodology should incorporate familiar and tailored billing mechanisms that free the current cost allocation of as much ambiguity as possible. Straightforward accounting not only benefits the accounting staff but also the customers. A customer should be able to understand how the charges are calculated, what increases and decreases these costs, and how differences in their operations affect how much and when the internal service fund charges impact their budgets. As an ISF initiates the Freeze step, major accounting and fiscal analysis must be performed for the fiscal team and management to accurately assess costs and how to reasonably allocate and bill those costs.

Fundamentally, an internal service fund's charges should be divided into either directly billable charges or non-specific core charges. When costs are easily identified, directly attributable to either an individual or a distinctive group of customers, and are a significant source of costs, then those ISF costs containing all three of those qualities should be billed directly to the customer. Economics plays an essential role in this determination. If costs are minimal and require meticulous tracking that costs more resources than they are worth, then these costs should not be directly billed to the customers and treated more like core (overhead) charges. During the Unfreeze period, an ISF needs to evaluate why it incurs costs and if those costs are due to a particular customer. For example, if an informational technology ISF pays for security software that can detect if emails contain malware, the ISF should ask, "Does this cost belong to one customer, or does IT security benefit all customers?" Security benefits all customers in the IT network, and therefore, the cost fails to be distinctly attributable to one customer. For another example, the Real Estate Management division asks IT to license, integrate, and maintain property management software. No other department wishes to utilize this software. Therefore, the IT department should separate this cost from other software costs and directly bill the fees and license costs the software company invoices IT to the Real Estate Management division. Costs should be meticulously evaluated and categorized into directly billable and or core charges. During the categorizing process, the ISF fiscal team members need to work alongside ISF program managers to appropriately label the costs and receive their operational perspectives to assess the feasibility of the new cost allocation methodology. Once all charges are categorized, only new charges need to be categorized further.

If costs do not possess all the qualities of a directly billable charge, then these costs should be incorporated into a charge table to promote more efficient cost accounting and more simplistic billing. A charge table is a billing practice where all non-directly billable charges are summed together and then divided among all customers using a certain bulk allocation methodology. For an ISF that provides building maintenance for their entire organization, their charge table may take all non-directly billable costs and assign a portion of those costs based on the square footage a customer occupies. A customer that occupies multiple buildings with enormous square footage will receive a larger bill than a customer sharing a small building space with other customers.

When determining how to assign costs to departments, ISFs need to consider equity when determining how many separate charge tables are developed and the allocation within each charge table. Equity considerations should encompass the unique characteristics of the customers a particular ISF provides services and/or goods to. Customer size, budget, billing timing, and funding flexibility stand out as top priorities when considering wealth disparities between customers. A key advantage of charge tables is that they offer a fixed allocation and amount for the budget year, and these charges are known to the customers when developing their budgets. Billable charges are subject to more variability as the usage of items depends on a particular department's needs. If for instance, smaller customers keep protesting surges of directly billable charges that their budget cannot handle during the budget year, then an ISF should consider switching the billable services to a core charge table to spread these costs more evenly to the customers. A charge table can help promote stabilized costs throughout the year and spread overhead charges more evenly to customers. Switching to a charge table for select services can help small customers afford services without fear of an unexpected billable cost exploding their budget.

While determining whether costs are directly billable and how the charge tables are created, the ISF staff should produce a written guide that lists what criteria were used to evaluate costs so that processes can be repeated and future staff and customers can learn the practice. By utilizing a segmented and structured Unfreezing step, the period allows an ISF a formalized opportunity to create a tangible rulebook and prevents staff from inconsistently applying a billable charge to a particular customer or across all customers. An acknowledgment must be incorporated as well that formalizes a process to review new costs as they are incurred and what to do in the interim of a budget year. If questions exist with certain costs, then this allows an opportunity to consult customers on how they view the charges and how to identify and allocate directly billable costs. Throughout the criteria discussions, all levels of ISF management need to be invited to offer their perspective and concerns. The establishment of a written procedure document limits previous management discretion. By integrating middle management's input, new procedures will find more success in being properly implemented, therefore, increasing reliability over charges. An ISF previously suffering from a lack of customer confidence can gain ground with customer trust through consistent billing practices. While categorizing all costs during the Unfreeze period seems daunting, proper cost accounting allows efficiency to be gained from preexisting labeled costs, consistent billing practices, and only updating the new charges during the following budget preparation.

Changing ISF practices should come swiftly as heavy preparation in the Unfreeze step allows a more seamless transition to the new billing practices. The Change step should occur during the actual ISF budgeting cycle where the new budget year's expenses are allocated using the newly devised methodology. ISF customers need to be informed that the change is going live and reminded about the benefits of the change. Following the Change step, the Hold and Update phase adds a cushion of time where the previous methodology is still being implemented from an accounting standpoint but an ISF is ready to shift at the start of the budget year. As older practices are phased out and discontinued, such as closing as many tickets for prior billable work, program operations should be geared to handle the change in methodology. This period is vital since it allows the opportunity to perform a trial run to discover any potential operational issues with the new billing practices and develop solutions to resolve them.

The start of the budget year signifies the transition to the final step, Freeze. New billing methodologies should be fully integrated into practices, and the implementing ISF should enter into a business-as-usual mindset. Important to note, ISFs need to honor any outstanding work under the previous billing methodology. If work was promised to fall under the charge table that is now billable, then the ISF should not bill the customer. The ISF should not bill newly billable work if an outstanding work order is unfinished when the ISF transitions to a new billing methodology. The ISF should absorb these transitional costs to promote a more welcoming atmosphere as the customer must navigate the changing costs. While addressing these last remnants of the previous practice, the ISF should reinforce how the updates will change these transactions. As soon as new transactions begin hitting customers' funds, overexplained messages calling out the change and new charges should signify that the ISF's organizational change is completed, and this is what the customer should come to expect.

Since Lewin's (1947) change model centered around communication, the revised model seeks to tackle current transparency issues with internal service funds head-on. The Freeze step of the model affords a period where dialogue between ISF and customers must be established and cultivated. Interdepartmental round table meetings to discuss ISF services and billing methodology offer ISF customers the chance to be heard and supported. With perhaps prior unchecked management discretion and secretive billing methodologies, customer satisfaction, and ISF management creditability could be at miserable levels. Therefore, previously discussed considerations should be incorporated into the structure of the meetings for both the ISF and the customer to articulate their perspectives about funding, current or future needs, and the quality of the services. If customers can see the impact of the billing methodology based on their feedback and niche circumstances, then better relationships can be formed during this Freeze period. The ISF should present a basic billing structure that considers their available resources that then can be shaped by customer input to create buy-in. Once a billing methodology is produced, the ISF needs to create a formal guidebook outlining services tied to rates while also defining a procedure to address niche circumstances.

Although the majority of the upfront customer participation should be completed during the Freeze section of the revised model, the subsequent steps provide an opportunity for feedback and insight from customers. Every subsequent transaction during the Change and Hold and Update steps should indicate that the billing falls under the previous cost allocation. At the start of the budget year and the Freeze step, ISFs need to present and explain the new transactions and what to expect throughout the year.

Section VI: Conclusion

This policy report provides recommendations to internal service funds to improve billing methodology and transparency to their customers utilizing a revised Lewin's (1947) model while highlighting certain considerations to incorporate into their organizational change.

While researching and detailing this policy report, the need for a nationwide survey and previous audit analysis of current ISF practices was apparent. A nationwide survey of cost allocation methodology, customer satisfaction, and current difficulties ISFs are confronting would provide a much more comprehensive and comparable data set to conduct qualitative and quantitative analysis. Much of the literature review cites sources from many decades ago when ISFs were attracting much more attention than today. Newly compiled data can reinvigorate discussion about the current ISF climate. An established data set with continuous yearly updates would allow accountants and researchers to more accurately gauge the state of internal service funds and provide more catered solutions to their issues.

For internal service funds to improve billing methodology and transparency with customers, significant resources, effort, and time must be dedicated to achieving material results. Knowing that financial reporting and financial health do not solely rely on accountants, ISFs, and customers must coordinate together to increase understanding, accountability, and clarity of charges to make more informed financial and operating decisions. This policy report contributes to the topic of ISFs by detailing a structured approach for ISF management to improve their current billing methodology practices and transparency utilizing an accommodating change model structure while providing examples and analysis of considerations to influence their change.

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