

Cost Studies

Expenditure Types & Audit Support

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http://finance.caltech.edu/Cost_Studies/Training_Materials

Overview

1. Why Recording Costs Correctly is important
2. Allocable vs. Allowable Costs
3. Selecting the Correct Expenditure Types
4. Supporting Audit of Allowable Expenses
5. DCAA Review of Facilities Costs
6. Capital Equipment versus Building Improvement Projects

Terms

- UG: 2 CFR 200, Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards typically called Uniform Guidance or UG
- Award: Document or documents that state terms, conditions, restrictions
- F&A rate: Facilities and Administrative, or “Federal Overhead” indirect cost rate.

Why is it Important to Select the Correct Expenditure Type?

Federal government

- Defines costs as allowable or unallowable for reimbursement.
- Requires that federal funds not be used to pay unallowable expenses so these types of expenses may NOT be charged either directly or indirectly to the federal government.

Why is it Important to Select the Correct Expenditure Type?

1. All expenditures at Caltech, regardless of funding source, must be coded appropriately to enable campus administration to determine if the expense is UG allowable or unallowable so that expenses can be appropriately included or excluded from indirect cost (F&A) rate calculations.
2. More than half of Caltech's research funding is from federal sources so the government wants to ensure that the F&A charges that are applied to the federal awards only include allowable expenses.

Myth: It matters less how you treat costs charged to a Caltech Funded Award

1. It is equally important that charges to Caltech funded awards are treated correctly, because all charges are brought into the calculation of the F&A rate and then treated as excluded, indirect or direct costs.
2. The government pays a portion of Caltech funded costs through the F&A Rate. Auditors scrutinize these costs as much as the charges to federally funded projects.
3. Government auditors review transactions charged to any funding source because they know that the presence of allowable and unallowable expenses impacts the F&A rate.

All Employees who Processes Transactions Need to Know how to Select the Correct Expenditure Types

The integrity of the data in Caltech's financial system depends on the knowledge and skill of each individual who processes financial transactions.

To comply with Caltech's obligation to the federal government for both direct and F&A or indirect cost recovery, staff and faculty must understand

- The distinction between allowable and unallowable costs and
- How to code and categorize expenses correctly

Our ability to obtain federal grants and contracts is dependent upon meeting federal requirements.

All Employees who Processes Transactions Need to Know how to Select the Correct Expenditure Types

It is highly recommended that staff involved in processing expense transactions be familiar with the cost allowability information described in UG Subpart E, and Caltech's accounting policies and procedures.

Unless staff is familiar with UG Subpart E, it is very likely that there are some expense transactions that are recorded in the incorrect expenditure type, or are treated inconsistently.

When in doubt, always ask the appropriate office regarding the correct expenditure type to use (OSR, PAA for Sponsored Awards, Financial Services for Other Awards).

Allocable vs. Allowable

Allowable Costs: Whether a cost is allowable depends on the funding source, Caltech policy, and in some cases, the terms & conditions of specific award where the costs will be recorded.

Costs are allowable to a project if:

1. The costs are reasonable;
 - a. Would a prudent person pay this amount for this item?
2. The costs are allocable to the specific project;
3. The costs are treated consistently in like circumstances; and
4. The costs conform to any limitations of the UG or the sponsored agreement.

Allocable vs. Allowable

Allowable Costs: Can be different under different funding sources and specific awards.

1. Only costs that are allowable under the UG and can be charged to federally sponsored awards directly or indirectly.
2. Costs that are normally unallowable under the UG can be allowable on awards that specifically identify the cost as being allowable.
3. Costs that are unallowable under the UG, but are an allowable Caltech expense cannot be charged to a sponsored award, unless it meets (2).
4. Costs that are not allowed by Caltech, the UG, or a specific award, are considered “Personal” expenses, and if these expenses are recorded in Caltech’s financial system, then they need to be reimbursed by the employees.

Allocable vs. Allowable

When is a cost allowable to charge to Caltech?

- Expenses must
 - Serve a legitimate Caltech business purpose.
 - Be supported by adequate explanation and documentation.
- Legitimate Caltech business purpose must
 - Support or advance the mission of the Institute which is to expand human knowledge and benefit society through research integrated with education.

Allocable vs. Allowable

When is a cost not allowable to charge to Caltech?

- Personal expenses are incurred for personal reasons or convenience and serve no legitimate business purpose.
 - These expense can be reimbursed or paid by Caltech only in extraordinary circumstances.
 - Require approval of the Office of Financial Services.
 - Employees need to reimburse Caltech for any unapproved personal expenses flowing through the financial system.
 - The reimbursement needs to be posted as a credit to the same PTA and expenditure type where the original expense was posted so they offset and net to zero.

Allocable vs. Allowable

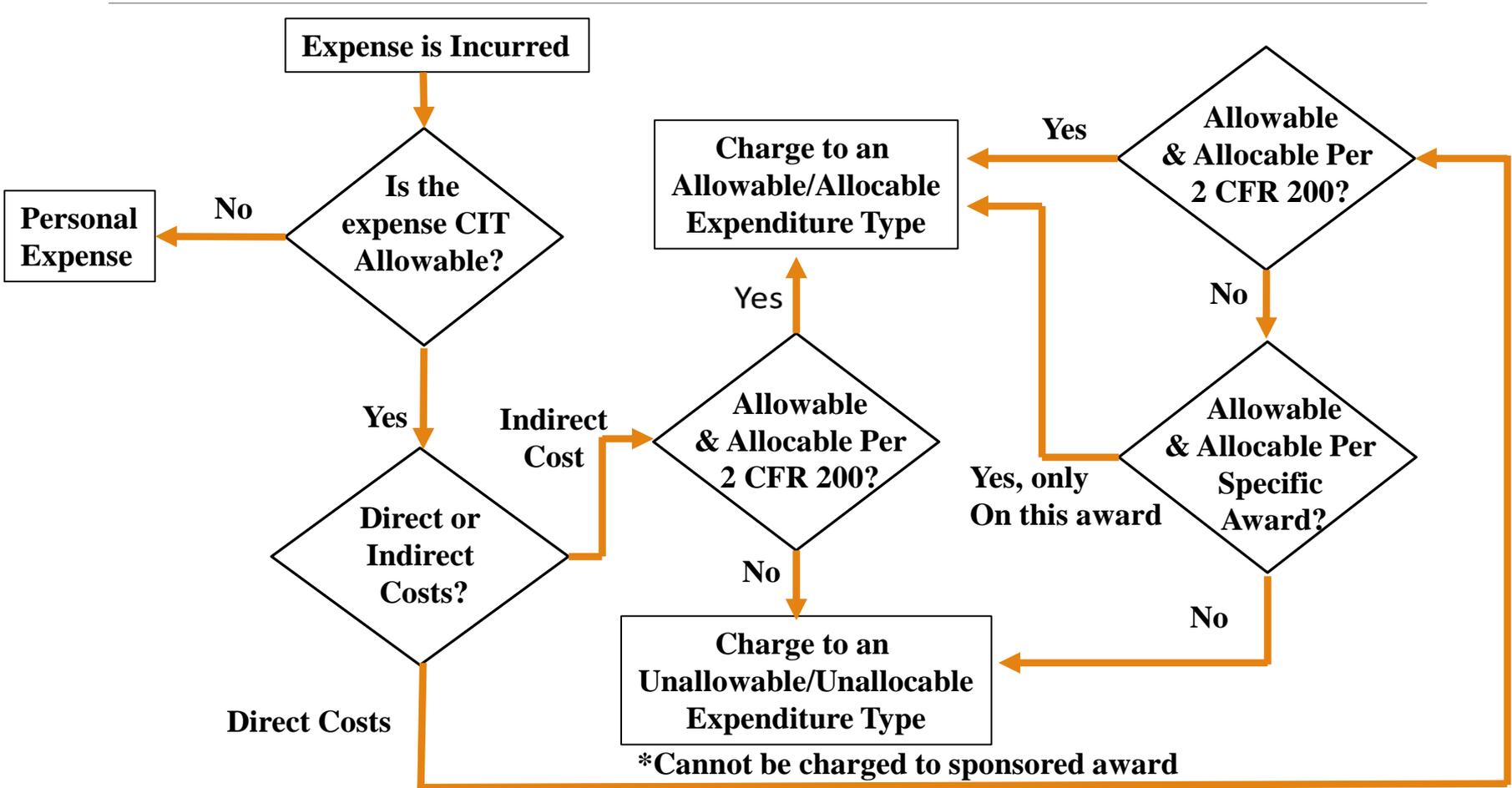
Allocable Cost: A **cost** is **allocable** to a project if goods or services involved are chargeable or assignable in accordance with the relative benefits received by the projects. In order to be allocable, a cost must meet the following criteria:

1. Relative benefits must be based on reasonable methodologies, and result in reasonable accuracies.
2. Reasonable methodologies means use of verifiable data, assumptions, and is mathematically correct.
3. Treated consistently in like circumstances.

Expenditure Type Flow Diagram (simplified)

Note 1: Direct Costs are normally charged to Sponsored Awards, Gifts, Grants, Endowments

Note 2 Indirect Costs are normally charged to Institute or to discretionary non-sponsored awards



Choices of Expenditure Types

Expenses that are allowable under the UG are also allowable as a Caltech expense. In these cases, use allowable, or “allocable” expenditure types. For example,

- ✓ Supplies-Allocable
- ✓ Travel-Domestic Allocable
- ✓ Consulting Fees-Allocable
- ✓ Dues-Allocable

Choices of Expenditure Types

Expenses that are allowable as a Caltech expense may UG may be unallowable under the UG. In these cases, use only “Unallocable” expenditure types. For example,

- ✓ Supplies-Unallocable
- ✓ Travel-Domestic Unallocable
- ✓ Consulting Fees-Unallocable
- ✓ Dues-Unallocable

Note: These unallocable expenditure types cannot be used to charge and expense to a sponsored award.

Choices of Expenditure Types

- **Bar:** Bar charges from the Athenaeum billed to their customers. Athenaeum use only
- **Catering Services:** Food and services provided by an external vendor for an event where the services extends beyond just delivery of the food (does not address allowability or allocability)
- **Entertainment:** Expenses for entertainment must be directly related to, or associated with, the active conduct of official Caltech business.
 - Expenses include meals, light refreshments, meeting space, amusement, diversion or social activities, including outings to night clubs, theaters, or sporting events. Related costs such as tax, transportation, gratuity would also be charged to this expenditure type. Detailed support documentation is required.
 - Alcohol - If approved for reimbursement to the employee, alcohol costs on travel expense reports must be segregated on payment requests and travel expense reports and charged to the 'Entertainment' expenditure type so that these costs can be treated as unallowable for F&A rate development purposes.

Choices of Expenditure Types

Food

- **Supplies-Allocable:** Irregularly scheduled lunch or evening dinner where there is a tight schedule and there is a business necessity for the meeting to take place at that time (a list of participants and their affiliation as well as an agenda, or note of topics discussed, should be available as support documentation).
- **Supplies-Unallocable:** Meals or Snacks for regularly scheduled lab meetings (e.g. bagels, donuts, cookies, pizza, sandwiches) where the meeting lasts more than hour.
- **Food:** Cost of food supplies incurred at the Athenaeum for the purposes of preparing meals for their customers. Athenaeum use only as these are not charges billed to their customers.

Choices of Expenditure Types

Meetings and Conferences

- **Mtgs and Conf Exp-Allocable:** Costs of locally (within 50 mile radius of Caltech) hosted meetings and conferences when the primary purpose is the dissemination of technical information or serves Caltech's business purposes are allowable. Allowable costs include meals, transportation, rental of facilities, and other items incidental to such meetings or conferences.
- **Mtgs and Conf Exp-Unallocable:** Costs of locally (within 50 mile radius of Caltech) hosted meetings and conferences that are not allocable under applicable cost principles, i.e. community, civic, or lobbying meetings.

Note, alcohol served at a meeting or conference hosted by Caltech must be charged to entertainment and appropriate documentation provided to support the costs. See Business Expense Guidelines – Entertainment and associated FAQs.

Choices of Expenditure Types

Travel

- **Travel-Domestic Allocable:** Travel costs incurred for an individual on official Institute business within the United States that are allocable under the UG.
- **Travel-Domestic Unallocable:** Travel costs incurred to take a trip or journey within the United States that are not allocable under the UG..
 - Airline upgrades from economy to a higher class of service and seat upgrades.

Choices of Expenditure Types

Travel

- **Travel-Foreign:** Travel costs incurred for an individual on official Institute business outside the United States where the travel is compliant with the Fly America Act and Caltech requirements related to it.
- **Travel-Foreign Unallocable:** Costs incurred to take a trip or journey within the United States that are not allocable under the UG.
 - Airline upgrades from economy to a higher class of service and seat upgrades.

Choices of Expenditure Types

Travel

- **Travel-Non US Carrier:** Use of non-US Carrier, not allocable under applicable cost principles whether for domestic or foreign travel.
- International travel on non-US carrier that does not comply with the Fly America Act and Caltech requirements related to it.

Choices of Expenditure Types

Fees and Dues

- **Fees:** Services performed by professionals (other than consulting).
- **Consulting Fees:** Fees charged for professional or technical services by non-employees that are retained by the Institute.
- **Consulting Fees-Unallocable:** Fees charged for professional or technical services by non-employees that are retained by the Institute that are not allocable under the UG.
- **Dues:** Dues charged by organizations that are allocable under the applicable cost principles.
- **Dues-Unallocable:** Dues charged by organizations that are not allocable under the UG.
 - For example, memberships in a civic or community organization, country club, social, dining organization, or organization whose primary purpose is lobbying.

Choices of Expenditure Types

Equipment Lease and Rental of Equipment

- **Leased Equipment:** Equipment lease payment on a capital lease as defined by FASB. Lease usually has an option to buy the equipment as part of the agreement. If the value of the agreement exceeds \$500K, then it is considered a capital lease and is capitalized.
- **Rental of Equipment:** Equipment rental payment under an operating lease as defined by FASB. No option to purchase and is treated as an ordinary lease so the costs are not capitalized.

Choices of Expenditure Types

Cost of Sales

- **Cost of Sales:** FOR USE IN INVENTORY CENTERS ONLY-Costs related to the sale of inventory
- **Facilities Cost of Sales:** Facilities-Cost of Sales. Used only by the Facilities Department.

Choices of Expenditure Types

Link to a more comprehensive list of expenditure types:

http://finance.caltech.edu/documents/511-expenditure_type_matrix_for_sponsored_awards.pdf

For Brief Descriptions of Any Expenditure Type, go to:

<https://financial-queries.caltech.edu>

Support Documentation

What kind of information and documents are needed to support an allowable expense?

Support Documentation

Here are some of the documents DCAA is requesting during the transaction testing part of the audit field work:

1. Purchase Requisition (or equivalent approval document)
2. Request for Bid, Sole-Source Justification, Price Justification
3. Purchase Order and/or Purchase Contract
4. Proof of Receipt of Items Purchased
5. Invoice
6. Proof of Payment (e.g., copy of check payment)

Note: DCAA may request other documents depending on the transaction and how it is processed.

Support Documentation

Who is responsible for retaining the original support documents?

How long do we need to keep the original documents?

Is a vendor's quotation considered adequate support documentation?

Support Documentation

1. DCAA expects Caltech to provide visibility of all information appearing in the support documents that allows them to easily verify all ORACLE transaction amounts they are testing.
2. DCAA will not spend much time trying to figure out how to reconcile dollar figures, and will ask Caltech to do this for them when they are unable to do this easily; otherwise, unreconciled costs will be questioned and treated as unallowable.
3. This means, as an Institute, Campus needs to place more effort into ensuring that the official documents they are using to support expenses can be easily translated into the dollar amounts appearing in the ORACLE transactions.
4. Going forward, it is likely more audit support may be needed from the Campus departments to assist in reconciling ORACLE figures to the support documents if the those documents can't be easily reconciled to the transaction information.

Support Documentation

1. Invoices: Information on the invoice needs to clearly show what line items make up the individual transaction amounts recorded in ORACLE in a PTA and expenditure type.
2. If the invoice includes both capital and non-capital items then the invoice needs to show which line items are capital equipment and which are not.
3. If the invoice includes more than 1 capital equipment item, then the invoice needs to show which line items are associated with each capital equipment.
4. If this information is missing, the vendor should be asked to send a revised invoice prior to making the final payment
5. Alternatively, the department purchasing the items can include internally created support (Excel) with the invoice that shows all the line items on the invoice and totals showing which lines add up to each capital and non capital item by expenditure type.

Support Documentation

Invoices: Information on the invoice needs to clearly show what line items are capital equipment.

If the invoice line items combine equipment items that are not the same or did not cost the exact same amount:

- The information needs to be split out by line and documented so that it is clear what the cost is for each asset in order for the assets to be properly recorded in Oracle Fixed Assets.
- This can be accomplished using internally created support (Excel) which shows all the line items on the invoice and totals showing which lines add up to each capital and non capital item by asset and expenditure type.

Support Documentation

Business meetings, lunches, activities, or events may need to be supported by the following:

1. Description of the business purpose of the meeting, lunch, activity, or event.
2. Description of the subject being addressed during the event
3. Include a list of participants and/or type of participants
4. Meeting agenda, and/or meeting minutes
5. For a meeting occurring during meal time where a meal is provided, a reason why the meeting had to be conducted at that time
6. Recurring or periodic business meetings during meals are more scrutinized
7. Conferences and training should include explanations as to how the event or individual's attendance at the event would benefit Caltech

DCAA Review of Facilities O&M Costs

Because O&M belongs to the non-capped Facilities component of the F&A rate, DCAA spends an enormous amount of time reviewing O&M costs.

1. Are the costs allowable under 2 CFR 200 cost principles?
2. Were transactions processed consistent with Caltech's written policies and procedures?
3. Can Caltech provide all of the supporting documents from the start to the end of the entire procurement process?
4. Is the dollar amount verifiable and correct?
5. Is DCAA able to see these dollar figures recorded in the ORACLE Financial System?

DCAA Review of Facilities O&M Costs

What are some of the O&M Costs being questioned:

1. Expenses associated with holiday events
2. Membership fees and dues related to unallowable purposes
3. Personal expenses where we cannot easily identify reimbursements from the employee
4. Car rentals, parking fees, chauffeur services where there is an absence of a business purpose
5. Items purchased for working lunches
6. Travel expenses
7. Capital equipment (mostly furniture items meeting Caltech definition of equipment) charged as materials under non-capital building improvement projects

Examples of High Risk Expenses

1. Birthday cakes, cards, celebrations, flowers, gifts
2. Food expenses
3. Retirement celebrations
4. Employee Service awards, employee recognition events
5. Office Bottled water /Water Dispenser subscriptions
6. Annual Association Membership fees
7. Magazine or Journal Subscriptions
8. Cable TV subscriptions
9. Fingerprinting Services & Drug Testing
10. Residential pool care costs

DCAA Review of Facilities O&M Costs

Note: Capital equipment should not be charged to a Capital Facilities Improvement PTA (e.g., PLFC). If this happens,

1. Assets meeting the definition of capital equipment rather than fixed equipment charged to a capital facilities improvement account will be included in the capitalized project costs and treated as a single building improvement or land improvement asset, and this is incorrect.
2. This is also non-compliant with CAS 501 requirement regarding consistency in treatment of costs.
3. Capital equipment may be recorded in a non-capital building improvement project because the asset will be capitalized as equipment so there will be no concern with the equipment being absorbed into a building asset.

Equipment Definition

Caltech's Definition of Capital Equipment

A capital equipment is movable item which has a cost that meets the following criteria:

1. An acquisition cost of \$5,000, or more, **AND**
2. A useful life of more than one year, **AND**
3. A stand-alone item (fully functional on its own, and not attached to a structure to function properly)

Equipment Definition

Acquisition Cost

Includes the following: Invoice amount, sales tax, freight/shipping costs, installation costs, costs for the initial complement of supplies needed to place the asset into service, accessory and auxiliary apparatus necessary to make it usable for the purpose for which it was acquired; less trade or trade in discounts and/or educational allowances.

Excludes the following: Federal Excise tax, duty, insurance, maintenance and warranty costs

Cost Studies Contact Information

http://finance.caltech.edu/Cost_Studies

Renee Cowan – x8104

Evan Prochaska-X4428

Linda Zhong – x3788

Jessica Solorzano– x8015

Ted Lieu – x2579

Ginger Baker – x2540