

EXTERNAL AUDIT CIRCULAR No. 4



CONNECTICUT DEPARTMENT OF TRANSPORTATION

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SUBJECT: Advertising and Selling Costs

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This Circular presents interpretative guidance regarding advertising and selling costs and includes examples for use in determining the allowability of such costs. Please refer to Chapter 8 and 6.3B of the 2010 edition of the AASHTO Uniform Audit & Accounting Guide for additional guidance.

I. DEFINITIONS

As used in this Circular—

1. "Advertising" includes all activities related to promoting the sale of products or services, regardless of the medium employed, when the advertiser has control over the form and content of what will appear, the media in which it will appear, and when it will appear. Advertising media include but are not limited to conventions, exhibits, free goods, samples, magazines, newspapers, trade papers, direct mail, dealer cards, window displays, outdoor advertising, radio, and television.
2. "Direct selling" refers to activities engaged in to induce particular customers to purchase particular products or services of the consultant. Direct selling is characterized by direct, person-to-person contact and includes such efforts as familiarizing a potential customer with the consultant's products or services, conditions of sale, and service capabilities. It also includes negotiation, liaison between customers and the consultant's personnel, technical and consulting efforts, and individual demonstrations, and any other efforts having as their purpose the application or adaptation of the consultant's products or services for a particular customer's use.
3. "Bid and proposal costs" means the costs incurred in preparing, submitting, and supporting bids and proposals (whether or not solicited) on potential Government or non-Government contracts. Generally, bid proposal costs are allowable as indirect expenses on contracts to the extent that those costs are allocable and reasonable.

II. ISSUE

During an indirect cost rate audit of a consultant, the auditor may encounter advertising and/or selling costs that are included in the consultant's indirect costs. Allowability criteria for each type of cost are discussed below.

A. ADVERTISING COSTS

Advertising costs are allowable if required for contract performance (e.g., ads placed to acquire scarce items and ads placed to dispose of scrap materials) or when used as a tool for recruiting new employees. Since contracts between the Connecticut Department of Transportation (CTDOT) and consultants

primarily involve professional services, generally the only advertising costs that may be included in a consultant's indirect cost rate are costs associated with help-wanted advertising. The allowability of the costs is subject to the following restrictions:

1. Help-wanted advertising that fails to describe specific positions or classes of positions is unallowable.
2. Advertising that is excessive in relation to the number and importance of the positions, or in relation to the practices of the industry, is unreasonable and therefore unallowable.
3. Help-wanted advertising that includes material that is not relevant for recruitment purposes, such as extensive illustrations or descriptions of the company's products or services, is unallowable.

B. DIRECT-SELLING COSTS

Although most costs associated with marketing must be removed from indirect costs, direct, person-to-person selling costs incurred prior to contract award are allowable. These efforts include familiarizing a potential customer with the consultant's product or services, conditions of sale, and service capabilities. Reasonable costs associated with direct selling are allowable, provided that the consultant provides support for the costs. The supporting documentation must include the following:

1. An expense report with itemized receipts,
2. The name of the firm's employee who initiated the direct-selling effort,
3. The target of the effort, and
4. The subject of the discussion, including the specific project discussed.

III. EXAMPLES

Example 4-1. At the consultant's request, advertisements were placed in a telephone directory and several magazines.

Analysis: These costs are unallowable.

Example 4-2. A consultant paid dues for its membership in various civic and community organizations.

Analysis: These costs are unallowable.

Example 4-3. At a conference, a consultant rented a hospitality room and offered refreshments.

Analysis: These costs are unallowable.

Example 4-4. A consultant prepared brochures to distribute at seminars and conventions.

Analysis: These costs are unallowable.

Example 4-5. A consultant's employee or agent hosted a lunch with local city officials to discuss the firm's expertise. No specific project was discussed.

Analysis: These costs are unallowable.

Example 4-6. At a consultant's request, help-wanted advertisements were placed in a local newspaper. The advertising was aimed at building a backlog of resumes, rather than filling specific job openings.

Analysis: These costs are unallowable.

Example 4-7. At a consultant's request, help-wanted advertisements were placed in a local newspaper. The advertising described the positions being offered, the compensation and fringe benefits, desired qualifications for applicants, and included a brief description of the company and its work.

Analysis: These costs are allowable.

REFERENCES

- FAR 31.205-1 (advertising costs required for contract performance).
- FAR 31.205-34 (help-wanted advertising as an allowable recruitment cost)
- DCAA Contract Audit Manual § 7-2104 (help-wanted advertising).
- FAR 31.205-38 (selling costs).
- CTDOT External Audit Circular No. 1 (definitions, audit authority, and general guidance regarding the computation of indirect cost rates).
- AASHTO Uniform Audit & Accounting Guide [2010 Edition]