July 9, 2015

FOSTER CARE AUDITS AND RATES LETTER NO. 2015-01

TO: ALL GROUP HOME PROVIDERS
    ALL COMMUNITY TREATMENT FACILITY PROVIDERS
    ALL FOSTER FAMILY AGENCIES
    ALL REGIONAL CENTER GROUP HOMES
    ALL REGIONAL CENTER FOSTER FAMILY AGENCIES
    ALL COUNTY WELFARE DIRECTORS
    ALL CHIEF PROBATION OFFICERS
    ALL COUNTY MENTAL HEALTH DIRECTORS

SUBJECT: AUDIT GUIDE FOR PREPARING FOR A FISCAL AUDIT

Enclosed is an Audit Guide for Non-Profit Organizations (NPO) that receives Federal Title IV-E Aid to Families with Dependent Children – Foster Care (AFDC-FC) funding. The purpose of this Audit Guide is to provide NPOs with a basic understanding of fiscal audits performed by the California Department of Social Services (CDSS), Foster Care Audits and Rates Branch (FCARB). Specifically, the Audit Guide offers technical assistance for preparing for a fiscal audit, identifies common issues that may cause audit findings, and offers recommendations for strengthening internal controls and documenting expenditures. Also, the information may be useful for improving the Board of Director’s oversight. However, the Audit Guide is not intended to address all fiscal audit requirements or to replace the advice of your tax, corporate, audit or other professionals or to be relied on as an authoritative guide for passing a fiscal audit.

Please feel free to contact the FCARB audit staff at (916) 653-1802 regarding any questions related to the Audit Guide for further clarification of the information provided or to obtain additional information.

Sincerely,

(Original Signed By)

CHERYL TREADWELL, Chief
Foster Care Audits and Rates Branch
Children and Family Services Division

Enclosure
c:  California Alliance of Child and Family Services
    Community Residential Care Association of California
    California Welfare Directors Association
    Chief Probation Officers of California
Audit Guide for AFDC-FC Funded Non-Profit Organizations

Helpful Information for Preparing for a Fiscal Audit

Presented By:
California Department of Social Services
Foster Care Audits & Rates Branch
Fiscal Year 2014/15
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ACKNOWLEDGEMENTS

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Disclaimer

This Audit Guide (Guide) is for Non-Profit Organizations (NPO) that receive federal Title IV-E Aid to Families with Dependent Children – Foster Care (AFDC-FC) funding. NPOs include those currently operating as Foster Family Agencies and Group Homes. The purpose of this Guide is to provide NPOs with a basic understanding of fiscal audits performed by the California Department of Social Services (CDSS), Foster Care Audits and Rates Branch (FCARB), also referred to as the federal awarding agency or pass-through entity/agency. It is not intended to address all fiscal audit requirements; to be relied on as an authoritative guide for passing a fiscal audit; or to replace the advice of your NPO tax, corporate, audit, or other professionals. This Guide offers recommendations for strengthening internal controls; documenting expenditures; improving Board of Director oversight, and it provides references that NPOs may use to find additional information. All references are current at the time of initial publication of this Guide, after which it is important to check all referenced citations.

An NPO is usually a non-profit corporation; however, it can be a trust, association, or a similar entity. This Guide discusses generally what is required of all NPOs and where language is specific to a corporation is used for simplicity. CDSS recommends that you seek advice from your legal and/or accounting professional for requirements specific to your organization. For example, Articles of Incorporation may also be Articles of Association, Articles of Organization, or Trust Instruments, etc.; Trustees may function as a Board.

You will note references to federal regulations that were effective December 26, 2014, located at Title 2 of the Code of Federal Regulations (CFR), Part 200\(^1\), that are applicable to entities that receive federal funding. The new law is also referred to as the Super Circular because it streamlines a number of Office of Management and Budget (OMB) Circulars, including familiar ones such as OMB A-122 (Cost Principles for Non-Profit Organizations) and A-133 (Audits of States, Local Governments and Non-Profit Organizations). Any new audit requirements in the Super Circular will apply to audits of NPO fiscal years beginning on or after December 26, 2014. The revised audit requirements are not applicable to fiscal years beginning prior to that date. For example, if an NPO’s fiscal year starts July 1, 2014 the Super Circular would not apply to the audit for the NPO’s fiscal year starting July 1, 2014, but would apply to the audit for its fiscal year starting July 1, 2015. Because there will likely be an overlap during the transition, this Guide will reference both current 2 CFR 230 for audits of fiscal years beginning prior to December 26, 2014 and 2 CFR 200 for audits of fiscal years starting after December 26, 2014. Where possible, the OMB references will also be cited.

It is recommended that NPOs seek the advice of their Certified Public Accountant (CPA) or other professionals specializing in the state and federal regulations governing NPOs, to assist with decision making regarding program operations, and preparation for an audit.

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\(^1\) See the Federal Register at [https://www.federalregister.gov/articles/2013/12/26/2013-30465/uniform-administrative-requirements-cost-principles-and-audit-requirements-for-federal-awards](https://www.federalregister.gov/articles/2013/12/26/2013-30465/uniform-administrative-requirements-cost-principles-and-audit-requirements-for-federal-awards)
Chapter 1 – Introduction

Purpose of the Guide

The purpose of this Audit Guide is to provide NPOs with basic information that will assist in the preparation for a fiscal audit, internal control, documentation and reporting requirements. Additionally, this Guide provides NPOs with technical assistance, which can increase the knowledge of state and federal rules governing NPOs and provide more awareness of expected compliance. Specifically, this Guide includes a helpful question and answer section based upon questions previously submitted by NPOs to the FCARB. Finally, there is a list of resources for NPOs seeking more specific information regarding meeting auditing requirements.

The accounting, expenditure, and internal control standards described in this Guide are basics. This Guide is not intended to be all inclusive, replace existing procedures or preclude the use of more sophisticated methods. Instead, this Guide discusses suggested procedures and controls that can be incorporated into an NPO’s business practices and aid in the goal of meeting state and federal fiscal requirements.

Throughout the process of accounting, record keeping, reporting and auditing, a NPO must follow Generally Accepted Accounting Principles (GAAP); 2 CFR 200.49 defines GAAP as having “the meaning specified in accounting standards issued by the Government Accounting Standards Board (GASB) and the Financial Accounting Standards Board (FASB).” However, FASB is the controlling standard for non-governmental entities.

Applicability of Law – Transition

New regulations at 2 CFR §200 will replace NPO requirements for (1) Administrative Requirements formerly found in the OMB A-110 and 2 CFR 215; Cost Principles from OMB A-122 and 2 CFR §230; and Single Audit Requirements from OMB A-133. Language from OMB 87 is also merged for consistency among federal instructions.

The new guidance streamlines the language from eight existing OMB circulars (the applicable OMBs are discussed in this document) into one document, hence the reference, “Super Circular!”

3 http://www.gasb.org
4 http://www.fasb.org/home
5 Financial Accounting Standards Board (FASB) has been the designated organization in the private sector for establishing standards of financial accounting that govern the preparation of financial reports by nongovernmental organizations.
Non-Profit Organizations Authority Timeline:

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2 CFR §200

Subpart A (§200.000) – Acronyms and Definitions
Subpart B (§200.100) – General Provisions
Subpart C (§200.200) – Pre-Federal Awards Requirements and Contents of Federal Awards
Subpart D (§200.300) – Post Federal Award Regulations
Subpart E (§200.400) – Cost Principles
Subpart F (§200.500) – Audit Requirements

Purpose of a Fiscal Audit

The purpose of a fiscal audit is to evaluate the financial condition of an NPO that receives federal AFDC-FC funds to provide foster care services to children in out-of-home care, to determine whether the program funds were spent on allowable and reasonable costs, that expenditures have the appropriate documentation, and that the NPO complies with all applicable state and federal statutes and regulations related to the program operations. The auditor is required to report any deficiencies, called findings, (2 CFR §200.516) and include these in the schedule of findings and questioned costs.

Scope of a Fiscal Audit

The scope of the audit (2 CFR §200.514) is determined by, but not limited to the evaluation of the NPO’s Financial Audit Reports (FARs) and cost data. This evaluation may warrant a full fiscal review on one or more fiscal years, or a more limited scope if a particular area(s) seems to be noncompliant. For example, if the FAR and/or cost data demonstrate a weakness in documenting capital expenditures; or failure to allocate personal and NPO use of business vehicles and/or equipment; or unpaid payroll taxes, then the scope may be, but not necessarily be, limited to those identified areas.
It is also possible that the scope will broaden to other areas as the auditors conduct the audit. Moreover, FCARB auditors will request and review records related to expenditures, internal controls, reporting, record keeping and Board of Director (“Board”) oversight.

**Preparing for a Fiscal Audit**

Each NPO should ensure that the records for its program are clear, concise, maintained separately from other program operations, are well-organized and are made available to the FCARB auditors upon request. Program expenditures are expected to be well-documented and indicate the business purpose for each transaction.

Preparation for an audit should include review of:

- NPO’s internal controls;
- NPO written policies to ensure that they are accurate, up to date and followed consistently;
- NPO written policies and the manner in which the NPO Board of Director’s conducts oversight of the NPO;
- NPO revenue sources to ensure that they are easily identified to ensure that AFCD-FC funds are spent only on allowable expenditures;
- NPO expenditures to ensure that they are allowable, reasonable and necessary and well-documented;
- NPO Board minutes to ensure that major decisions were diligently considered, including contracts, leases, employment, loans, capital expenses, less-than-arm’s length transactions, etc.
Chapter 2 - Internal Controls

Internal controls are defined at 2 CFR §200.61 as “a process, implemented by a non-federal entity, designed to provide reasonable assurance regarding the achievement of objectives in the following categories:

(a) Effectiveness and efficiency of operations;
(b) Reliability of reporting for internal and external use; and
(c) Compliance with applicable laws and regulations.

Internal controls are designed to prevent fraud and clerical errors that may compromise the accuracy of an NPO’s financial statements. Internal controls should also ensure accuracy in finances/financial reporting; the safeguarding of NPO assets; and compliance with applicable state and federal laws, regulations and policies. The elements of a solid internal control system are focused on segregation of duties, access, authorization, reconciliation, record keeping, and reporting.

The 2 CFR §200.303 also addresses the importance of internal controls and requires that the NPO “establish and maintain effective internal controls” in order to ensure that the management and expenditure of a federal award is consistent with state and federal law and any award-specific requirements.

A NPO, through its Board, must establish clear, written guidelines for effective internal controls that will safeguard AFDC-FC funds received; and ensure that the AFDC-FC funds are used in the manner intended, and for the benefit of children placed in its care. Effective internal controls should include, but are not limited to, the following:

- Written Board-approved policies and procedures distributed to all staff;
- Separate recording and identification of sources of funding, including donations;
- Monthly reconciliation of bank accounts by someone other than the person authorized to approve expenditures, who signs checks or authorizes electronic payments;
- Segregation of payroll duties between the individual authorizing employment and compensation from the person who issues payroll;
- Recording of cash receipts immediately, depositing daily, reconciling, and maintaining with adequate security;
- Original receipt/invoice shall accompany all expenditures however made, including reimbursement of employee for NPO expenses;
  - If the original receipt/invoice is the type that may deteriorate over time (e.g. thermal print) then a copy must be made to preserve the information and attached to the original.
  - If the original receipt/invoice has been lost then a reliable substitute generated and provided directly by the vendor/merchant will be considered; such as a duplicate or an electronic receipt.
All receipts are required to contain an adequate description to determine what was purchased, the specified business purpose and the identification of NPO employee/purchaser in order to review for accuracy and reasonableness.

- Pre-authorization of disbursements (via checks or electronic payment) to vendors by management and reviewed by the Board;
- Disbursements made by check;
  - Are made on pre-numbered checks, used in numerical order, with accounting for blank or void checks;
  - Are not made payable to “cash” or signed in advance;
  - Have supporting documentation that references check numbers and marked “paid,” or otherwise canceled, to prevent reuse or duplicate payment and the original documentation is retained by the NPO;
  - Requirement of a second signature on all checks over a “significant” amount as defined in the NPO’s internal control policy.
- The petty cash fund is entrusted to a single custodian, must be adequately safeguarded, and each expenditure must be documented as to its business purpose. It is recommended that petty cash replenishment checks be made payable to the fund custodian rather than cash. The replenishment check shall only be issued in the amount equal to the total case disbursements supported by receipts.

**Internal Controls and Common Findings**

**Segregation of Duties**

Finding(s):

- The NPO fails to maintain a written policy regarding the segregation of duties; or
- The NPO fails to adequately address segregation of duties in its written internal controls policy.

Either may result in inconsistence in, or absence of, adequate segregation of duties procedures. This may result in financial transactions being handled by only one person, or a few, from beginning to end. Examples are (1) where the same person sets his or her own salary, manages his/her own hours and issues his/her own pay or (2) authorizes an expenditure, reviews the documentation for adequacy and issues a reimbursement check to themselves; or (3) an individual who performs bank reconciliations also handles cash, check writing, or bookkeeping functions.

An individual (and ideally not even a few individuals) should not be in a position to initiate, approve, undertake and review any one transaction from beginning to end. The NPO must avoid allowing complete control of funds, with no process for accountability to others in the organization as to decisions made on the expenditures. Different people should authorize payments, sign checks, record payments in the books, and reconcile the bank statements.
Small organizations can put in place effective segregation of duties. For example, one person (paid staff) signs the expenditure checks and a different person (e.g. Board Treasurer) reviews disbursements, bank statements, and cancelled checks on a monthly basis.

**Bank Reconciliation**

Finding:
- The NPO fails to conduct monthly bank reconciliations.

Ideally, monthly bank reconciliations are prepared within 30 days of the bank statement date; unreconciled items are resolved timely; are dated and signed by both the preparer and the reviewer, and reviewed by a member of the Board of Directors or its designee for appropriateness and accuracy.

**Petty Cash**

Finding(s):
- The NPO fails to establish an adequate executive management-approved written petty cash policy. The policy may not adequately set forth procedures that specify the amount authorized for the petty cash fund; the person responsible for maintenance of the fund; procedures for disbursement; or documentation expected for expenditures.
- The NPO fails to safeguard the petty cash fund. If a written policy is in place, the funds may not be kept in a secured or locked location. Absent or inadequate security allows unmonitored access to, and expenditures of, petty cash funds.

Petty cash allows the NPO to make small purchases or reimbursements, in cash, for items such as stamps, office supplies, etc. Petty cash should not be used as a substitute for normal purchasing and disbursement practices. When petty cash is used as a substitute for normal purchasing and disbursement practices the NPO can lose control and oversight over expenditures affecting determination of whether the expenditures are well documented, reasonable, necessary, and NPO-related. Original receipts/invoices are required and retained to avoid duplication, as well as other supporting documents that together indicate the item purchased, the employee making the purchase, and the NPO business purpose of the purchase.

The Board of Directors and senior management should develop a policy that sets the amount of available cash in the Petty Cash Account and a process for how it is to be replenished. For example, an amount of $100 should be sufficient for most small NPO’s business needs as the expenses to be covered are intended for small amounts. Using the example of a typical $100 petty cash fund, when the fund gets low, e.g. $20 remaining, the custodian (a bookkeeper or a member of the NPO staff) makes a request to management to replenish the petty cash fund.
The custodian verifies that the receipts match the amount needed to replenish - $80 - and an $80 replenishment check is issued to the fund custodian to bring the Petty Cash Account to its original amount of $100.

**Credit Card Use**

Finding(s):

- Failure of the NPO to monitor and control expenditures made with NPO credit cards resulting in unauthorized purchases that are unreasonable, unnecessary, and/or made for personal use.
- Failure of the NPO to require executive management pre-approval or similar failsafe for major credit card expenditures to assure the expenditures are reasonable, necessary, and business related.
- Failure of the NPO to require adequate supporting documentation for staff use of personal credits cards to make purchases on behalf of the NPO.
- Failure of the NPO to require and maintain original invoices; store receipts or other documentation; and credit card statement(s), which indicates the business purpose and the employee making the expenditure.
- Failure of the NPO to exclude the payment, with AFDC-FC funds, of interest on credits cards; of which is unallowable with AFDC-FC funds. Interest may be paid from adequately documented sources other than AFDC-FC funds.

The use of credit cards, both NPO issued credit cards and an employee’s personal credit card used on behalf of the NPO, should be limited to purchases where normal purchasing and disbursements practices are not suitable.

Credit cards issued in the NPO’s name must be adequately protected and the use monitored to ensure that only authorized and necessary items are purchased. Credit card purchases should be pre-approved by the NPO’s executive management, or a similar failsafe put into place, to ensure that purchases are reasonable and necessary.

As with any expenditure, an original receipt/invoice is required to accompany all credit card expenditures. If the original is subject to deterioration over time (e.g. thermal print) then, a copy may be made and attached to the original. If the original receipt/invoice has been lost, then a reliable substitute, generated by the vendor/merchant, will be considered; such as a duplicate or an electronic receipt. All receipts/invoices must contain an adequate description to determine what was purchased; the specified business purpose and the identification of the NPO employee/purchaser to enable review for accuracy and reasonableness. Credit card statements are not sufficient support for credit card purchases but can aid in the reconciliation. A receipt/invoice may establish a purchase with more detail than a statement, but a statement will also show credits for the return of items.
Chapter 3 - Board of Directors

Role and Authority

The Board of Directors (“Board”)\(^6\) is given the authority and responsibility for managing the NPO. The Board meets and makes decisions together and consists of the governing body members identified in the organizing documents (or bylaws) or assembled pursuant to instructions in the organizing documents. The Board is ultimately responsible for making sure the NPO is run properly. See the Cal. Corp. Code §§5210 through 5260.

Responsibilities

The Board, and each member, has a special legal relationship to the NPO called a fiduciary relationship. As fiduciaries, members of the Board must place the interests of the NPO before all other interests. To protect the NPO, the Board must guard against harm caused by any unfair or unreasonable transactions, conflicts of interest or self-dealing transactions. The Board must therefore take an active role in overseeing the NPO by performing important duties that include, but are not limited to, the following:

- Conduct regular meetings;
- Adhere to all federal and state laws applicable to the activities of the NPO;
- Make and approve both short and long-range goals and objectives;
- Develop an operating budget/financial plan to ensure adequate funds to meet immediate (expenses) and future needs (financial plan/insurance) of the NPO;
- Adopt policies and procedures;
- Protect the assets and interests of the NPO. Evaluate carefully any self-dealing transaction or potential conflict of interests in any transaction;
- Evaluate, compare/negotiate and approve terms of contracts;
- Oversee and test expenditures for compliance with state and federal laws, including review and approval of large expenditures such as the purchase or lease of real estate property, purchase or lease of automobiles, and capital improvements; and
- Evaluate the operation of the NPO and assure implementation and monitoring of internal controls.

Caution: A Board member is specifically prohibited from entering into a residential “shelter care” lease for property owned by the member, or for which the member will materially benefit (e.g. family member benefits). A self-dealing lease may result in forfeiture of the NPO's AFDC-FC rate. See Welf. & Inst. Code §11462.06(d).

\(^6\) Or other governing body of the private, nonprofit – Charitable Trust, (Trustees), Association (members), etc.
Role in an Audit

FCARB auditors will interview each board member as part of a fiscal audit to evaluate the Board member’s knowledge of the NPO, responsibilities, concerns, and awareness of the financial operation of the NPO and knowledge of laws applicable to the operation of the group home, foster family agency or other foster care organization. The Auditors will review Board minutes, resolutions, articles of corporation, and bylaws for compliance with the Cal. Corp. Code and compliance with other state and federal laws related to the conduct of the NPO business and applicable to the operation of a group home, foster family agency or other foster care organization. For this reason it is very important that all NPO actions are overseen by the Board and that all Board actions have well-documented support for its decisions. If an action was taken by the NPO without Board approval, such as an individual’s decision or a decision with less than a quorum of disinterested Board members, it is important that the Board review the transaction considering the facts at the time of the decision to determine whether the act was allowable, reasonable, and in the best interest of the NPO before ratifying that prior act or decision.

All group home board members are required to review CDSS’s booklet entitled “Facts You Need to Know Group Home Board of Directors”. This booklet has valuable information and examples of expectations for group home boards. It is also very instructive for foster family agencies and other foster care organizations as a guide on Board member responsibilities. However, do not rely solely on this publication for current law. Instead, refer to the Cal. Corp. Code §§5210 through 5260 when making decisions as a Board. Nonprofit corporate law as a whole is located in the Cal. Corp. Code §§5000 through 10841.
Chapter 4 - Expenditure Analysis

Applicable Regulations and Reminders

Federal regulations found in 2 CFR §200 establish uniform administrative requirements, cost principles, and audit requirements for federal awards to non-federal entities including NPO’s receiving federal Title IV-E funding. General Provisions for Selected Items of Cost commencing at §200.400 Cost Principles for NPO’s, along with CDSS regulations located in the Manual of Policies and Procedures (MPP) at 11-400 et. seq., specify allowable and unallowable costs for NPOs receiving federal AFDC-FC funding.

In order to be allowable under a federal grant, in accordance with 2 CFR §200.403, costs must be:

- Necessary and reasonable for performance of the grant;
- For shared costs, allocable to the grant;
- In conformity with any limitations in the Cost Principles, award terms and conditions and applicable law as to types or amount of cost items;
- Consistent with policies and procedures that apply uniformly to both federally-financed and other activities of the grantee/NPO;
- Accordeed consistent treatment by the grantee/NPO;
- Determined in accordance with GAAP;
- Excluded as a cost of, or used to meet match requirements of, another federally-funded program

The federal regulations at Subpart E of 2 CFR §200 describe the Cost Principles for NPOs and commencing at §200.420 list over 50 selected items of costs, define, detail them, and establish standards on whether the costs are allowable, not allowable, allowable under an exception, or allowable only if approved by the granting agency. It is the NPO’s responsibility to know, understand and comply with the general principles applicable to entities receiving federal funding and with the requirements specified in this Part.

If the NPO is uncertain whether a cost is allowable, the NPO may avoid subsequent disallowance or dispute based on unreasonableness or non-allocable, by consulting with FCARB in advance. However, the absence of an advance consultation will not, in itself, affect the reasonableness or allow-ability of that Cost Item. (2 CFR §200.407)
NEW in 2 CFR § 200 – new/amended selected cost items and requirements

Prior Written Authorization

All requirements for prior written authorization are now in one place at §200.407. Some of the common circumstances that must have prior written authorization from FCARB are the following:

- § 200.308 Revision of budget and program plans;
- § 200.445 Goods or services for personal use;
- § 200.430 Compensation—personal services;
- § 200.447 Insurance and indemnification;
- § 200.431 Compensation—fringe benefits;
- § 200.454 Memberships, subscriptions, and professional activity costs;
- § 200.438 Entertainment costs;
- § 200.458 Pre-award costs;
- § 200.439 Equipment and other capital expenditures;
- § 200.462 Rearrangement and reconversion costs;
- § 200.441 Fines, penalties, damages and other settlements; and
- § 200.474 Travel costs.

Written Policies

Some of the common cost items that generally require written policies are:

- § 200.430 Compensation—personal services;
- § 200.431 Compensation – fringe benefits;
- § 200.447 Insurance and Indemnification;
- § 200.463 Recruiting costs;
- § 200.464 Relocation costs; and
- § 200.474 Travel costs (this includes mileage reimbursement).

Selected Cost Items New and/or Amended.

Audit Services

(2 CFR §200.425; 2 CFR §230, App. B, Cost Item 4) – New audit threshold $750,000.00

Costs associated with the following types of audits are now specifically designated as unallowable:

- Audits not conducted in accordance with Single Audit requirements; and
- Audits that fall below the Single Audit threshold, which increased effective December 26, 2014, to $750,000.00.
Note: The new audit threshold applies to an NPO’s fiscal year commencing after December 26, 2014. For example, an NPO fiscal year that commences January 1, 2015 would be subject to the new audit threshold. However, a fiscal year commencing July 1, 2014 ending June 30, 2015 would not be subject to the new audit threshold until their fiscal year commencing July 1, 2015.

Compensation – Personal Services

The Super Circular changes how non-profits assess, track and allocate employee compensation costs for the purposes of their federal awards. Charges for employee compensation still must be based on records accurately reflecting work performed. However, no specific type of documentation – such as Personnel Activity Reports (PARs) which had been prescribed in Circulars A-122 and A-87 – is required. Rather, non-federal entities’ records must meet the following standards:

- Be supported by a system of internal controls which provides reasonable assurance that the charges are accurate, allowable and properly allocated;
- Incorporated into the non-federal entity’s official records;
- Reasonably reflect the total activity for which the employee is compensated;
- Encompass all activities – those that are federally assisted and those that are not;
- Comply with the established accounting practices and policies of the non-federal entity; and
- Support the distribution of the employee’s salary or wages among specific activities or cost objectives.

Only if the federal government finds that a non-federal entity has not met the Super Circular’s standards for documenting compensation may it require Personnel Activity Reports or equivalent documentation.

OMB removed language previously in Circular A-122 requiring prior approval to charge to a federal award overtime, extra-shift, etc.

Another change applicable to non-profits is the consideration of an additional factor when determining if the total compensation of an employee is allowable. The new factor to consider is whether the hiring of the employee is in accordance with a NPO’s rules or written policies and meets applicable federal requirements.

Compensation – Fringe Benefits
(2 CFR §200.431 – New to NPOs and now requires a written policy)

Following OMB Circular A-87’s lead, general language, new for non-profits, explains that the cost of fringe benefits is allowable provided the benefits are reasonable and required by law, and there is an employment agreement or an established policy.
The following criteria must be met for leave benefits (e.g., annual, FMLA, sick, holidays, court, military, administrative, etc.) to be allowable:

- Benefits are provided for under established written leave policies;
- Costs are equitably allocated to all related activities including federal awards; and
- Accounting basis selected for costing each type is consistently followed.

Also costs of pension plans and post-retirement health plans may be computed using a pay-as-you-go method or an acceptable actuarial cost method in accordance with established written policies.

**Conferences**


The Super Circular offers new guidance for non-federal entities that **host or sponsor** conferences. In an attempt to promote family-friendly practices, the Super Circular allows costs associated with **identifying**, but not providing, **locally available dependent care resources** to be charged to a federal award. It also requires conference hosts/sponsors to exercise discretion and judgment in ensuring that conference costs are appropriate, necessary and managed in a manner that minimizes costs to the federal award.

**Employee Health and Welfare Costs**


Employee morale costs are no longer allowable. OMB made this change because it concluded that such costs are difficult to distinguish from entertainment costs and potentially result in opportunities for waste, fraud and abuse.

**Entertainment Costs**


Generally, entertainment costs are still unallowable, but now certain costs may be charged to a federal award if they: (1) have a **programmatic purpose** and (2) are authorized either in the approved budget or with **prior written approval** from the federal awarding agency.

**Fines, Penalties, Damages and Other Settlements**


**All costs** (not just fines and penalties) resulting from alleged and existing violations and failures to comply with laws and regulations are disallowed. Such costs are allowed; however, when they are incurred as a result of compliance with federal award provisions or with **prior written approval** from the awarding agency.
Therefore, NPOs seeking to settle legal claims alleging violations of laws or regulations (such as employment discrimination claims) will need to obtain written prior approval from the awarding agency before using federal award funds to settle those claims.

**Materials and Supplies Costs**

As under existing OMB Circulars, materials and supplies used for the performance of a federal award may be charged as direct costs. However, the Super Circular clarifies that charging computing devices as direct costs is allowable for devices that are essential and allocable, but not solely dedicated to, the performance of a federal award.

**Memberships, Subscriptions and Professional Activity Costs**

New for non-profits is language stating that costs of membership in organizations whose *primary purpose* is lobbying are unallowable. This language derives from the OMB Circular A-87 and has been modified to refer to organizations whose *primary purpose* is *lobbying* rather than to those that are “substantially engaged” in lobbying.

**Rearrangement and Reconversion Costs**

Unlike the prior circulars and federal regulations, the Super Circular addresses whether rearrangement and reconversion costs are to be charged as direct or indirect. Now costs incurred for ordinary and *normal* rearrangement and alteration of facilities are to be charged as indirect costs whereas costs incurred for *special arrangements* and alterations are allowable as direct costs *if prior approval is received* from the pass-through entity, FCARB.

**Rental Costs of Real Property and Equipment**

The following definition of “*family members*” has been added for purposes of determining when a relationship between two parties will result in a less-than-arm’s-length lease (i.e., a lease under which one party to the lease agreement is able to control or substantially influence the actions of the other):

- Spouse, and his/her parents;
- Children and his/her spouse;
- Parents and their spouses;
- Siblings and their spouses;
- Grandparents and grandchildren and their spouses;
- Domestic partner and his/her parents; and
Any individual related by blood or affinity whose close association with an employee is equivalent to a family relationship.

Caution: This definition will expand circumstances that will lead to a material benefit of a Board member when the NPO enters into a lease for property owned by the member’s family. Another important reminder is that a self-dealing lease that involves residential “shelter care” may result in forfeiture of the NPO’s AFDC-FC rate. See Welf. & Inst. Code §11462.06(d).

A new “less-than-arm’s-length” disallowance is added that prohibits the use of federal money for rental of commercial or residential property for purposes such as a home office from anyone affiliated with the NPO.

GAAP provisions must also now be used for determining if a lease is a capital lease.

**Training and Education Costs**

The costs of training and education provided for employee development is now allowable for non-profits without the extensive analysis that was previously required. 2 CFR 230 contained requirements in seven paragraphs (a) through (g). 2 CFR 200.472 now simply says: “The cost of training and education provided for employee development is allowable.”

**Travel Costs**

New for NPOs is the requirement that methods used for charging travel costs must be in accordance with the NPO’s written travel reimbursement policy. Also, to charge travel costs (including lodging, meals and incidentals) of employees and officers to a federal award, documentation must justify that: (1) participation of the individual is necessary to the federal award; and (2) the costs are reasonable and (3) consistent with the NPO’s written established travel policy.

Consistent with efforts to promote family friendly policies, non-federal entities will have the option of using federal funds to cover temporary dependent care costs that directly result from travel to conferences as long as the costs are (1) A direct result of the individual’s travel for the award; (2) Consistent with documented travel policy; and (3) Only temporary during the travel period.

Travel costs for dependents are unallowable except for travel lasting six months or more with prior approval from a federal awarding agency.
Most Common Expenditure Findings

Alcoholic beverages

Alcoholic beverage costs are unallowable. There are no exceptions for business meals, holiday parties, gifts, etc.

Rental Costs of Buildings

Finding(s):

- Failure of the NPO to determine reasonable rental costs;
- Failure to ensure that self-dealing or less-than-arm’s-length lease agreements are treated properly to determine reasonable rental costs; and
- Failure to retain documentation of the determination of reasonable rental costs.

Generally, rental costs are allowable up to the fair market rental value (FMRV) of the property. The FMRV is allowable to the extent that the rates are reasonable in light of such factors as: rental costs of comparable property, market conditions in the area; alternatives available and the type; life expectancy; condition; and value of the property leased. However rather than using the FMRV, in circumstances that arise from a “sale and lease back” or “less-than-arm’s-length” lease transaction described in 2 CFR §200.465(b) and (c), the federal regulations limit the allowable cost of these leases to the “cost of ownership.” NPO’s must be aware that the federal regulations have become much more stringent, particularly with respect to leases entered into between the NPO and any individual or circumstance that would be “able to control or substantially influence the actions of the other.” These circumstances may arise from a “sale and lease back” or “less-than-arm’s-length” lease transaction described in 2 CFR §200.465(b) and (c). In any case, both of these types of leases are not allowed the FMRV, but are based on the “cost of ownership” had the NPO either retained or purchased the property respectively.

Free-market-lease, one with no related party or self-dealing transaction: (2 CFR §200.465(a) and Welf. & Inst. Code §11462.06(a)) rental costs are allowable up to the FMRV at the time the NPO entered into the lease. The NPO should retain:

- Appraisals;
- Evidence of comparable property or equipment;
- Property tax statements;
- Lease agreements; and
Any other documentation to assist the auditors to determine reasonableness of rental costs.

NOTE: In addition to the federal requirements, California imposes further restrictions. Welfare and Institutions Code (Welf. & Inst. Code) §11462.06 addresses the free-market, arm’s length residential “shelter care” costs for group homes. Specifically, subdivision (a) limits residential shelter care costs to 12% of fair market value (FMV) of the property at the inception of the lease or when the lease is renewed. This amount is annualized so the FMRV on a monthly lease is divided by 12. When comparing the monthly lease amount under this state law to the amount determined in 2 CFR 200.465(a), the FCARB will allow the lesser of the two amounts.

For sale/leaseback and less-than-arm’s-length lease transactions, see 2 CFR §200.465(b) and (c) respectively. The allowable lease amount for these is based on the “cost of ownership” rather than the FMRV.

Sale and lease back transactions: 2 CFR §200.465(b) addresses the “sale and lease back” scenario where the NPO buys a property, sells it, and leases it back to the NPO situation; this transaction is subject to the “cost of ownership” limitation. The rental costs under the “sale and lease back” arrangement are allowable only up to the amount that would be allowed had the NPO continued to own the property rather than enter into the lease. The analysis of the cost of ownership (here continued ownership) considers expenses such as depreciation, maintenance, taxes, and insurance as if the NPO had retained ownership of the property. The question is whether the NPO would have had a better deal (and lower cost to the federal grant) had the NPO retained ownership of the property.

Less-than-arm’s-length lease: 2 CFR §200.465(c) addresses another type of lease that uses the “cost of ownership” cost analysis. It is described in the federal regulations as a “less-than-arms-length” lease. This kind of lease is allowable only up to the amount that it would cost had the NPO held title to the property since the date the property was purchased. The same analysis as in 2 CFR §200.465(b) is applied, which considers expenses such as depreciation, maintenance, taxes, and insurance as if the NPO had ownership of the property since it was originally purchased by the lessor.

NOTE: Welf. & Inst. Code §11462.06(d)(1) states “(d) (1) … any group home provider with a self-dealing lease transaction for shelter costs, as defined in Section 5233 of the Corporations Code, shall not be eligible for an AFDC-FC rate.” However, even if the lease does not meet the state definition of a “self-dealing” lease transaction, it may still be a “less-than-arm’s-length” transaction under federal law. (See 2 CFR §200.465(c) above).
Records the NPO should retain for analysis of “cost ownership” for applicable lease/rental transactions pursuant to 2 CFR §200.465(b) and (c) include but are not limited to:

- Lease agreements;
- Copies of NPO licenses;
- Purchase price, property value for land and improvements, date of purchase, and interest rate;
- Owner’s annual depreciation for each property to support how depreciation was calculated. For example, documentation that includes the property values for land and improvements, the date of purchase, depreciation basis etc.;
- Annual interest payments such as the IRS form 1098 Mortgage Interest Statement;
- Annual Property Tax statements;
- Annual Property Insurance statements or invoices;
- Annual Property Maintenance records and Costs Worksheet; and
- Documentation of Board of Director approval for rental costs of real property and equipment including documentation the Board has assessed the reasonableness of the transaction.

Note home office prohibition: Finally, be aware a new “less-than-arm’s-length” disallowance is added that prohibits the use of federal money for rental of commercial or residential property for purposes such as a home office from anyone affiliated with the NPO. 2 CFR §200.465(c)(6).

**Equipment and other Capital Expenditures**

Finding(s):

- Failure of the NPO to obtain pre-authorization for capital expenditures;
- Failure of the NPO to obtain Board approval for capital expenditures;
- Failure of the NPO to adequately record decisions related to capital expenditures in the Board minutes.

**Capital expenditures must meet pre-authorization requirements.** Capital expenditures are expenditures to acquire capital assets or expenditures to make additions, improvements, modifications, replacements, rearrangements, reinstallations, renovations, or alterations to capital assets that materially increase their value or useful life. The federal regulations contain specific requirements depending on whether the expenditures are treated as direct or indirect charges. For example, capital expenditures for general-purpose equipment, buildings, and land are unallowable as direct charges, except with prior written approval by CDSS.
Capital expenditures for special purpose equipment are allowable as direct costs, provided that items with a unit cost of $5,000 or more have prior written approval from FCARB.

The NPOs must ensure that pre-authorization is obtained for capital expenditures; that the Board is thoroughly informed and approves and documentation in the minutes is recorded. The NPO should familiarize itself with relevant regulations effective December 26, 2014, including, but not limited to, those located at 2 CFR §200.13 Capital expenditures, §200.33 Equipment, §200.89 Special purpose equipment, §200.48 General-purpose equipment, §200.2 Acquisition cost, §200.12 Capital assets, §200.439 Equipment and other capital expenditures.

Compensation – Personal Services

Finding(s):

- Failure of the NPO to set reasonable compensation;
- Failure of the NPO to obtain Board approval and document in the minutes;
- Failure of the NPO to consider entire remuneration, besides salary, such as incentive awards, fringe benefits, pension plan costs, allowances for off-site pay, incentive pay, location allowances, hardship pay, and cost of living differentials;
- Failure of the NPO to consider outside available and reliable sources to determine reasonable compensation.

Compensation for personal services includes all compensation paid currently or accrued by the organization for services of employees generally rendered during the period of the award. It includes, but is not limited to, salaries, wages, director and executive committee member's fees, incentive awards, fringe benefits, pension plan costs, allowances for off-site pay, incentive pay, location allowances, hardship pay, and cost of living differentials. The NPO can use any available outside reliable source to determine reasonable compensation. FCARB uses the Child Welfare League of America salary study to determine reasonableness of salaries. FCARB recognizes there are other comparable salary studies. It is advisable to consult your CPA on whether or not a salary is considered reasonable.

The costs of compensation for personal services are allowable to the extent that: (1) the total compensation to individual employees is reasonable for the services rendered; (2) conforms to the established policy of the organization; (3) is consistently applied to both federal and non-federal activities; and (4) charges are adequately supported.
Incentive compensation or bonuses to employees based on cost reduction, or efficient performance, suggestion awards, safety awards, etc., are allowable to the extent that the overall compensation is determined to be reasonable and such costs are paid pursuant to an agreement entered into in good faith between the organization and the employees before the services were rendered, or pursuant to an established plan followed by the organization.

Note: A commonly misused expense is compensation for personal services for NPO-furnished automobiles. That portion of the cost of NPO-furnished automobiles that relates to personal use by employees (e.g. transportation to and from work) is unallowable as fringe benefits regardless of whether the cost is reported as taxable income to the employees. NPO-furnished automobile expenditures are allowable as direct costs to the AFDC-FC award when necessary for the performance of the AFDC-FC award and approved by the awarding or pass through agency (i.e. FCARB).

**Contributions**
(2 CFR §200.434; 2 CFR §230, App. B Cost Item 12)

Finding:

- Failure of the NPO to adhere to restrictions on the use of AFDC-FC funds for contributions.

Contributions and donations by the NPO to others are unallowable. Contributions or donations made by the NPO, including cash, property, and series, made by the organization, regardless of the recipients are unallowable. Gift cards to employees and tips are considered cash donations, unless gift cards are given to an employee in the form of a bonus, which is further discussed in the Employee Bonuses section below.

**Gifts/rewards/incentives for foster children**
(42 USC 675(4)(A))

Finding:

- Failure of the NPO to establish a gift-giving and/or incentive policy;
- Failure to seek prior approval when necessary; and
- Failure to maintain adequate documentation.

Reasonable gifts provided to children in care fall within personal and incidental costs attendant to foster care maintenance payment costs. If the gift is for accomplishments such as grades, graduation, etc. it would be allowable if it furthers the NPO purpose and is authorized prior to implementation.

In order to safeguard assets and ensure accountability, the Board should establish and approve a policy that specifies a scheduled plan for gift giving. The plan should be reviewed periodically, along with the program’s budget review process.
Other period gifts/rewards should also be included in a plan that is reviewed by the Board and has prior approval of the FCARB.

**Employee Bonuses**  
(2 CFR §200.437; 2, CFR, §230, App. B, Selected Items of costs, 8(j) and 13)

Finding:

- Failure of the NPO to establish an employee bonus policy and retain adequate documentation.

Costs incurred in accordance with the NPO's documented policies for the improvement of working conditions, employer-employee relations, employee health, and employee performance are allowable. Such costs are allowable to the extent that they are found to be reasonable, paid or accrued pursuant to an agreement entered into in good faith between the NPO and the employees before the services were rendered, or pursuant to an established plan followed by the NPO that is so consistent as to imply, in effect, an agreement to make such payment.

It is up to the Board of Directors to determine and approve if bonuses or other forms of compensation are reasonable and warranted. The Board of Directors must first establish and approve a reasonable, measurable written plan prior to the issuance of any such bonuses/ incentives.

The NPO should maintain, at a minimum, Board minutes, bonus policy, original receipts, invoices, ticket stubs, gift card numbers, proof of efficient performance, and any other documentation that may substantiate the transaction.

**Entertainment Costs**  

Finding:

- Failure of the NPO to adhere to the restrictions on entertainment costs.

Entertainment costs for employees, including amusement, diversion, and social activities and any costs directly associated with such costs such as tickets to shows or sports events, meals, lodging, rentals, transportation, and gratuities are unallowable. These costs may be paid from other sources of funding such as donations to the NPO.

An exception is where the entertainment costs might have (1) a *programmatic purpose* and are authorized under the federal award and (2) have *prior written approval* from FCARB. Entertainment costs associated with children in the care of the NPO are allowable as within the coverage of foster care maintenance payment costs as a personal and incidental cost.
However, the expenditures will still be evaluated for reasonableness. For example, a field trip to Disneyland from Los Angeles would likely be considered reasonable whereas a field trip to Disney World in Florida would not.

**Fines and Penalties**

Finding:

- Failure of the NPO to adhere to the prohibition on the use of AFDC-FC funds for the payment of fines and penalties.

Fines and penalties resulting from violations of or failure of the organization to comply with federal, state, and local laws and regulations are unallowable except when incurred as a result of compliance with specific provisions of an award or instructions in writing from the awarding agency. Examples of items disallowed under this provision include but are not limited to, bank overdraft fees, non-sufficient fund fees, tax fines, tax penalties, parking tickets, late fees and excess mileage fees on car leases.

**Goods or Services for Personal Use**

Finding:

- Failure of the NPO to adhere to the prohibition on the use of AFDC-FC funds for goods and services for personal use.

Costs of goods or services for personal use or benefit by the NPO’s employees are unallowable regardless of whether the costs are reported as taxable income to the employees. Examples: non-business-related meals paid with NPO funds. NPO credit card charges used to purchase goods or services that are personal, personal cell phones paid with AFDC-FC funds.

**Travel Costs (including Mileage)**
(2 CFR §200.474; 2 CFR §230, App. B Cost Item 51a)

Findings:

- Failure of the NPO to establish and implement a written travel policy;
- Failure of NPO to apply the correct mileage rate for volunteers (unpaid staff);
- Failure to adhere to restrictions on the use of AFDC-FC funds for employee travel costs; for example:
  - Failure to exclude commuter miles, which are not allowable, is the most common finding.
Failure to exclude travel costs for family or other companions who accompany an employee on NPO business-related travel, e.g. flights for spouses, sons and daughters; and

- Failure of the NPO to adhere to requirements for documentation for the use of AFDC-FC funds specifically for mileage reimbursement.

Travel costs are the expenses for transportation (including mileage), lodging, subsistence, and related “incidental” items incurred by employees who are traveling on official business of the NPO.

Incidental costs are those reasonable and necessary expenses that are incurred related to lodging and subsistence while traveling for business. All travel costs will be reviewed to verify they are necessary to carry out the purposes of the AFDC-FC funding, are reasonable, and consistent with the NPO’s written travel policy.

Mileage

A written travel plan must be in place to ensure compliance with state and federal law.

NPO employees and/or volunteers have two options when it comes to deducting car expenses. They can choose from the Standard Mileage (57.5 cents for 2015) deduction method or the Actual Car Expenses deduction method. Please check the Internal Revenue Service (IRS) site for the most recent and accurate information, regarding rules and rates related to reimbursement for the costs of operating an automobile for business or charitable purposes. Regardless, both methods require accurate records be kept as evidence for the deductions.

Under the Standard Mileage deduction, the miles are multiplied by the IRS deduction rate to determine the amount of the deductions. Actual expenses for things like gas, insurance and maintenance are not deducted, because they are factored into the mileage reimbursement rate. Track the miles then simply take the mileage rate multiplied by the reimbursable miles.

The “actual expenses method” is used for "itemizing" the actual cost of owning, maintaining and using the vehicle for business purposes. If the vehicle is owned and used 100% for business, then all of these costs can be deducted. In cases where the business use is less than 100%, only a percentage of the total expenses can be deducted. The employee must determine actual costs to operate the car for the portion of the overall use of the car that is business use. Include gas, oil, repairs, tires, insurance, registration fees, licenses, and depreciation (or lease payments) attributable to the portion of the total miles driven that are business miles. See IRS publication 510 on this subject. There are many specific requirements including when the reimbursement to the employee is taxable and when it is not.

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It is advisable to consult with the NPO accountant if this method is going to be used rather than a mileage reimbursement system.

For Charity and Non Reimbursed Business Use

The reimbursable mileage rate for charitable volunteers is not the same as for employees. The Internal Revenue Service establishes reimbursable mileage rates. (14 cents for 2015). Volunteers must keep the same accurate records of mileage as is required of employees. Mileage reimbursements are often disallowed due to a failure to maintain adequate documentation of the business purpose, and the failure to prohibit reimbursement for personal use.

The auditors will review mileage reimbursement to verify the reasonable and necessary official business use of the NPO. Documentation shall include the business purpose for each trip, to/from location, and total mileage traveled. The mileage reimbursement rate must comply with IRS standards. The best practice is to maintain mileage logs that document these facts and assure that all staff, including executive staff, comply with maintenance of logs.

Example mileage policy:

The NPO will reimburse employees for the use of their personal vehicle used for NPO business. Reimbursement will be at the then effective date and rate published by the Internal Revenue Service.

Mileage reimbursement is meant to cover only those miles incurred above and beyond the employee’s normal commute to his/her place of business. For example, if the normal commuting round trip is 20 miles, and the employee goes on a trip that covers 75 miles, only the incremental 55 miles are reimbursable. The number of days should also be taken into account. If the 75 miles in the above example were incurred over three business days, then the incremental reimbursable miles would be 15 (75 – (3 * 20)).

Reimbursement requests should at a minimum indicate the date of travel; purpose of travel; beginning and ending points of travel; reasonable and necessary parking (not tickets) and toll charges; and the miles eligible for reimbursement. If actual expenses, in lieu of the standard reimbursement rate for mileage, are reimbursed then original itemized receipts shall be submitted along with the travel claim.

Interest

Finding(s):

- Failure of the NPO to understand and apply the restrictions on the use of AFDC-FC funds for interest payments; and
• Failure to recognize that interest on credit cards or equipment rental is unallowable.

Interest costs incurred on borrowed capital or temporary use of endowment funds, or on the use of the NPO’s own funds, however represented, are unallowable. However, financing costs (including interest) to acquire, construct, or replace capital assets are allowable, subject to conditions specified in 2 CFR 200.449. For example, there are multiple requirements in 2 CFR 200.449 (c) such as: interest costs associated with the acquisition of facilities and equipment are limited to fair market value; from an unrelated (arm’s length) third party; the financing is obtained from an unrelated (arm’s-length) third party; and the interest cost is the least expensive alternative.

**Lobbying**


Finding(s):

• Failure of the NPO to understand and apply the restrictions on the use of AFDC-FC funds for lobbying; and
• Failure to understand that costs for membership in organization whose primary purpose is lobbying is unallowable.

Costs associated with lobbying activities are unallowable. See related 2 CFR §200.454; 2 CFR §230, App. B Cost Item 30. Memberships in organizations whose primary purpose is lobbying are unallowable.

**Professional Services**


Finding(s):

• Failure of NPO to make determination that contracting with a consultant is more cost effective than using an employee;
• Failure to document determination to use a consultant;
• Failure to evaluate consultant contracts to establish reasonable and necessary compensation; and
• Failure to document evaluation of contract and determination of reasonable compensation.

Costs of professional and consultant services rendered by persons who are members of a particular profession or possess a special skill, and who are not officers or employees of the organization, are allowable, when reasonable in relation to the services rendered and when not contingent upon recovery of the costs from federal funding. If the service professional is hired as a consultant rather than performing services as an employee, consider whether the service could have been performed more economically by direct employment rather than contracting.
Other considerations include the qualifications of the professional and the usual fees charged by that individual or entity, the industry standard rate; the adequacy of the contract including the description of service; estimate of time required; rate of compensation, and termination provisions.

Some professional consultants may include accountants, information technology specialists, and attorneys.

**Defense/prosecution: criminal/civil proceedings, claims, appeals and patent infringements**

**Finding(s):**

- Failure of the NPO to differentiate allowable and unallowable legal costs; and
- Failure to ensure that unallowable payment of attorney fees is not made for audit appeals that are lost or settled.

Attorneys have additional considerations/limitations. Generally, grant funds may *not* be used to litigate patent infringement or Major Fraud Act private party suits; defend an action brought under federal contractor and grantee whistleblower protection laws, unless the grantee wins.

For actions involving the government, generally, grant funds *cannot* be used to prosecute claims against the federal government. Nor can grant funds be used to defend the grantee/NPO in proceedings brought by government if the grantee/NPO loses, or in most cases, settles; unless the legal costs are specifically allowed in the settlement agreement. However, generally, grant funds *may* be used to defend the grantee in proceedings brought by government if grantee wins.

There are no general rules that restrict the use of grant funds for private suit legal fees (nongovernment). See the OMB response to comment in 1998 revision of A-122, which stated that legal fees incurred in defense of lawsuits not brought by [a government], except suits by former employees under Major Fraud Act, are allowable (63 Fed. Reg.104 at 29795).
Chapter 5 - Post Audit Actions
(OMB A-133; 2 CFR § 200.516)

The auditor will review the NPO financial statements, schedule of expenditures, and internal controls. If there are any material concerns in accordance with generally accepted accounting principles the auditor will make audit findings known to the NPO including the identification of questioned costs and how they were computed. The auditors will also look at whether these are repeat findings from a prior audit; and will determine recommendations to prevent future repeat findings.

Management Decision Letter
(OMB A-133; 2 CFR §200.521 (MDL); Welf. & Inst. Code §11466.2(c)(2))

After the completion of the fiscal audit field work, the auditors will allow 15 calendar days from the exit conference for the NPO to submit additional documentation to address the preliminary audit findings. The auditors will incorporate the NPO’s responses/additional documentation into a Management Decision Letter (MDL). The MDL is written notification sent to the Agent for Service of Process of the NPO, the President of the Board of Directors, Executive Director, and county-placing agencies regarding CDSS’ final audit findings (and corrective actions required.)

Corrective Action
(OMB A-133; §2 CFR 200.521 MPP §11-405.231(b))

The NPO has 60 days from the date of the MDL to comply with corrective action. Evidence that corrective action has been achieved will be supported by the NPO submitting adequate documentation regarding the specific actions required in the MDL. Failure to substantially comply with expected corrective actions may result in the termination of the NPO’s AFDC-FC rate.

Appeal
(MPP §§11-402.57; 11-405.232; and 11-430.12)

The NPO has the right to file an appeal regarding any audit findings identified in the final MDL within 30 days of issuance. The appeal will be heard in a formal hearing before an Administrative Law Judge (ALJ) within 60 days of receipt of the request for hearing. After completion of the hearing, a Proposed Decision and Order is issued by the ALJ to CDSS for consideration. CDSS has the authority to adopt the Proposed Decision and Order as a final Decision and Order, remand for additional evidence, or issue an Alternate Decision based on the record of the proceedings. If the NPO does not file an appeal within 30 days of issuance of the MDL, the audit findings in the MDL are considered final on the 31st day and any findings and disallowed costs are sustained and collectible.
Overpayment Collections

Voluntary Repayment
(Welf. & Inst. Code §11466.22(d)(3); MPP §11-402.66)

Once disallowed costs are sustained and collectible, a demand letter is issued for repayment of the sustained overpayment resulting from the fiscal audit, plus any accrued interest. The NPO shall enter into a repayment agreement within 30 (thirty) days of the demand. The repayment can be paid in a lump sum in accordance with MPP §11-402.66 or as a voluntary installment repayment agreement. The minimum monthly repayment by installment shall be 3 percent of the program’s monthly income and shall not exceed 9 years for full repayment of the overpayment amount including interest. (Welf. & Inst. Code §11466.22(d)(3)).

Involuntary (Mandatory) Repayment
(Welf. & Inst. Code §11466.22(d)(2) and MPP §§11-402.664 and 11-402.665)

If the NPO does not submit a lump sum payment; enter into a voluntary repayment agreement within 30 days of demand; or misses any three payments under a voluntary repayment agreement, CDSS shall submit the provider to mandatory (involuntary) repayment procedures. Under a mandatory repayment schedule monthly adjustments are made to your paid rate until the outstanding overpayment is repaid. The minimum monthly repayment shall be 5 percent of the program’s monthly income and shall not to exceed 7 years for full repayment of the overpayment amount including interest.

In addition to the repayment reduction of MPP §§ 11-402.664 and 11-402.665, the law further provides that 50% of any California Necessities Index (CNI) increases and any adjustments to the Standardized Schedule of Rates in the AFDC-FC program will be withheld and applied the overpayment; and the GH/FFA program will be ineligible to receive program change that results in an increased rate classification level (RCL) unless a waiver is granted.

Interest
(Welf. & Inst. Code §11466.25)

Interest for all sustained overpayments begins to accrue on an NPO provider overpayment on the date of the issuance of the final audit report pursuant to Welf. & Inst. Code §11466.25).

Community Care Licensing Actions

The Community Care Licensing Division (CCLD) of CDSS is copied on all audits conducted by FCARB. Depending on the findings in the audit, it is possible that CCLD will conduct further evaluation of the program for compliance with laws applicable to licensed Group Homes and Foster Family Agencies, particularly those related to financial malfeasance. FCARB may also review any CCLD actions or coordinate efforts with CCLD.
Chapter 6- Questions & Answers

NOTE: The following Questions & Answers Section is NOT an official guideline for your specific issues. Depending on the unique facts surrounding each question, there may be a modified or different response. This section is only intended to provide general guidance to help understand and prepare for a fiscal audit.

Questions

1. Are Internal Control procedures the same as an Employee Handbook?
2. Are Bylaws the same as Internal Controls?
3. We run a very small program and the Executive Director has complete control/knowledge of the organization and approves all purchases and transactions. Why are you asking us for our Internal Controls procedures?
4. Are receipts always necessary?
5. Do we have to keep receipts for small purchases such as those under $100.00?
6. What if the original receipt is faded?
7. What if the original receipt is lost or faded and I did not copy it?
8. Is a receipt all I need to support the expenditure?
9. What kind of supporting documentation do I need if the purchase receipt is insufficient?
10. Will the auditors accept itemized credit card statements or cancelled checks as sufficient documentation for purchases in lieu of original receipts?
11. If we note down the children’s name on receipts, are the purchases going to be automatically allowed?
12. Can items be purchased with cash?
13. Is there a limit to the amount of cash in a “petty cash” account and what types of purchases can be made with petty cash?
14. Do petty cash fund purchases need to be approved?
15. Can cash transactions be done with lump sum withdrawals or checks written to cash, from a bank account?
16. Who is ultimately responsible for all purchases, including those made with “petty cash”?
17. When are dual signatures recommended?
18. Why are we required to conduct bank reconciliation when the accountant is already aware of all transactions?
19. **Who issues or signs the payroll checks?**
20. **Can the Executive Director sign his/her own payroll check?**
21. **Does the Board have to approve the payroll check for the Executive Director?**
22. **What if a Board member is paid or reimbursed? Who issues the check?**
23. **Is there a compensation limit for the Executive Staff?**
24. **What is compensation?**
25. **What is the difference between allowable, unallowable and unsupported costs?**
26. **Are there special requirements for capital expenditures? And what are capital expenditures?**
27. **Can the NPO obtain pre-approval/pre-authorization from the State when it is uncertain about the allowability of a special or unusual cost?**
28. **Can the NPO purchase a vehicle?**
29. **What type of documentation must be maintained to support the allowability of an acquisition or lease of a vehicle?**
30. **Can the Board assign NPO-purchased or leased automobiles to staff?**
31. **The group home requires 24/7 care and the Executive/Administrative staff are on call 24/7. Do we still need to keep mileage logs when everything we do is childcare related?**
32. **Why was the NPO’s purchase of a Mercedes or Escalade that was assigned to an executive staff member, disallowed when it was exclusively used for business purposes of the NPO?**
33. **The vehicle assigned to the Executive Director needs repairs. Can s/he get a rental car?**
34. **Can the NPO use AFDC funds to pay for penalties issued by the federal, state, and/or county agencies?**
35. **Can staff, administrative or line, attend industry-related conferences/seminars (in state and out-of-state)? What type of documentation is needed to support the costs?**
36. **If the NPO has a credit card account and/or line of credit to meet the daily needs of the NPO, and interest charges are a part of the credit card contract, are the interest payments allowable?**
37. **Are bank fees allowable?**
38. **If the Staff members are using their personal vehicles for business purposes, can the NPO reimburse them for the repairs to their personal vehicles?**
39. **Can the NPO hire a handyman to perform routine repairs and maintenance to the facility?**

40. **Are hand-written receipts for these routine repairs acceptable as supporting documentation?**

41. **Can we throw a holiday party for our staff and children? Can we take our staff and children for an expensive dinner for special occasions?**

42. **We would like to purchase special door prizes such as IPADS, Nooks, etc. for an approved holiday party. What type of documentation is needed to justify the costs?**

43. **The NPO took the children to a well-known amusement park in California for an outing. Is this an allowable cost? If yes, what type of documentation is required for reimbursement?**

44. **The NPO took the children and staff on an overnight trip to San Francisco to tour the city and its sights. Some of the vendors such as the Alcatraz Tours do not provide receipts. How can the NPO prove that the children went to San Francisco when they are no longer in placement?**

45. **Can the NPO sign a contract for outside services a member of the Executive Staff and/or Board owns the company?**

46. **If children would benefit from having a recreation room in the group home, can we use AFDC-FC funds to convert the garage?**

47. **One of the children broke the kitchen countertop. Since it needs to be repaired, can the NPO upgrade the countertops to granite since it will be more durable?**

48. **Can AFDC-FC funds be used to pay for professional memberships, subscriptions?**

49. **Can AFDC-FC and other funds be commingled? The NPO operates other related programs with different sources of funding. The NPO also organizes a yearly fund-raiser to help defray the costs of running a group home. Since all the money raised is used to benefit the children, can we deposit the money in the same account as the AFDC-FC funds?**

50. **Can the NPO use AFDC-FC funds to donate to a cause related to their program?**

51. **Is there a limit to rental/lease costs?**

52. **What is a “self-dealing” or “less-than-arm’s-length transaction”? Is there a difference?**

53. **Are the requirements the same for “self-dealing” or “less-than-arms-length” lease/rental costs?**

54. **What if the lease is for a “residential shelter care cost”?**

55. **What type of documentation is required for lease agreements?**
56. **What happens if we are not using the entire facility leased for our group home; or one of our group homes (three in the program) is not being used at all? Is there an impact on the allowability of the rent/lease?**

57. **Can AFDC-FC funds be used for cash gifts/gift cards/ bonuses/other incentives to boost employee morale?**

58. **Can a Board member hold different offices at the same time?**

59. **Can the members of the Board be held responsible for the wrongdoings of an Executive Director and/or staff if they were not aware of the wrongful actions?**

60. **Can the members of the Board be compensated for their services?**

61. **Can family members serve on the Board at the same time?**

62. **What is a quorum?**

63. **What is the definition of an “interested party?”**

64. **How often is the Board supposed to meet?**

65. **What are the responsibilities of each Board Member?**

66. **Can the NPO lease a commercial facility from the Executive Director or a Board Member; and how is fair market rent determined?**

67. **Can the NPO lease a residential facility from the Executive Director or a Board Member; and how is fair market rent determined?**

68. **Can the auditors consider overall success of the program and or the happiness and success of the children in placement to mitigate any disallowed costs/findings?**

69. **How does the payment plan work? Who do we contact to discuss a payment plan?**

70. **Are the Board members and/or Executive Staff personally responsible to reimburse the State for any overpayments that result from a fiscal audit?**

71. **We have been in business for quite some time and have never been audited. Why now?**

72. **Can the NPO use AFDC-FC funds to repay the disallowed costs that result from a fiscal audit?**

73. **Can the NPO rate be terminated or its licensed revoked because of audit findings?**
Questions and Answers

1. **Are Internal Control procedures the same as an Employee Handbook?**

   No. Internal controls are the overall processes the NPO performs to ensure it achieves control of its operations and finances/financial reporting, safeguards its assets, and is in compliance with applicable laws and policies. The elements of a solid internal control system are focused on protection of assets by segregation of duties; access; authorization; reconciliation record keeping and reporting. Internal controls may be found in a stand-alone document or as part of a more general over-all employee or workplace handbook. In addition, Board minutes, memoranda, and other documents or correspondence may establish the organization’s methods for effecting internal controls.

   On the other hand, an employee handbook is generally a compilation of personnel policies and procedures, benefits, workplace expectations, etc. An employee handbook may provide documentation on the internal controls used by the NPO but it may not be the primary documentation that evidences internal controls.

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2. **Are Bylaws the same as Internal Controls?**

   No. Bylaws contain information about the rules and regulations that govern a corporation. Cal. Corp. Code §§5150-5153. Bylaws generally deal with governing issues such as: Organizational purpose, board structure, officer position descriptions and responsibilities, terms of board service, officer/board member succession and removal, official meeting requirements, membership provisions, voting rights, conflict-of-interest policy. To the extent that Bylaws address the internal organizational structure of the NPO, it has some inherent internal control elements.

   Internal controls, on the other hand, are processes and policies the NPO has in place to ensure compliance with applicable laws, regulations and policies. Fundamental to adequate internal controls is the safeguarding of its assets through segregation of duties, access; authorization, reconciliation, record keeping and finances/financial reporting.

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3. **We run a very small program and the Executive Director has complete control/knowledge of the organization and approves all purchases and transactions. Why are you asking us for our Internal Controls procedures?**

   Regardless of size, NPO’s receiving federal funds must maintain internal control over their operations.
Even a small program is expected to have a functioning Board of Directors and staff who can comprise an adequate separation of duties to ensure safeguarding of assets and internal controls designed to prevent fraud and clerical errors that may compromise the accuracy of an NPO’s financial statements. A foundational element of an adequate internal control system is the segregation of duties. In a small NPO this may seem problematic. However, no one person should have complete control of the NPO.

4. **Are receipts always necessary?**

   Yes. The original receipt/invoice is the minimally required form of documentation for all expenditures. NPOs are expected to obtain and retain clear legible receipts for all expenditures.

5. **Do we have to keep receipts for small purchases such as those under $100.00?**

   Yes. Original receipts must be retained for all expenditures regardless of the dollar amount.

6. **What if the original receipt is faded?**

   If the original is the type that may deteriorate over time (e.g. thermal print) then a copy must be made to preserve the information and attached to the original.

7. **What if the original receipt is lost or faded and I did not copy it?**

   NPOs are expected to obtain and retain clear legible receipts for all expenditures. If the original is illegible or has been lost then a reliable substitute generated such as a duplicate or an electronic receipt and provided directly by the vendor/merchant will be considered but not necessarily accepted.

8. **Is a receipt all I need to support the expenditure?**

   No. The original receipt/invoice is the minimally required form of documentation for all expenditures. Auditors will review all receipts to see if they contain a description adequate to determine who purchased the item, and whether that purchase was allowable; reasonable, well-documented, necessary and has a valid NPO business purpose.
However, if the receipt alone does not provide that level of detail then other supporting documents that together indicate the required information must be included.

Supporting documentation may include: canceled checks, original cash register receipts, original contracts, account statements, credit card sales slips, invoices, and petty-cash slips for small cash payments.

9. **What kind of supporting documentation do I need if the purchase receipt is insufficient?**

You may make contemporaneous notations directly on the receipt, such as a child’s name purchaser’s name and NPO purpose. Or an NPO may have a form that is used to contemporaneously document the purchase. The receipt and notations, forms, or supporting documentation together must allow the FCARB auditor to determine whether the purchase was reasonable, necessary and for a valid NPO business purpose.

10. **Will the auditors accept itemized credit card statements or cancelled checks as sufficient documentation for purchases in lieu of original receipts?**

No, a credit card statement alone will not be sufficient but will help to document an expenditure. As with any expenditure, an original receipt or invoice is required to accompany all credit card expenditures. All expenditures must be supported by adequate documentation to determine what was purchased, the specified business purpose and identification of NPO employee/purchaser to enable review for accuracy and reasonableness. Credit card statements are not sufficient support for credit card purchases but can aid in reconciliation. For example, a credit card charge of $422.00 at Target does not detail what was purchased or whether the purchase had a legitimate NPO purpose. A receipt will show more detail of the purchase, while the credit card statement will show credits for return of items.

11. **If we note down the children’s name on receipts, are the purchases going to be automatically allowed?**

No. While, contemporaneously made notations on the receipt will help support the business purpose, the name of a child alone will not be adequate to support the particular expense. The auditors will determine whether a given expense is allowable; that is, reasonable, well-documented, necessary and for the benefit of the child or other valid NPO business purpose. Receipts alone, even with the name of a child, do not automatically establish all of these criteria.
12. Can items be purchased with cash?

Yes. However, it is recommended that only small, incidental items be purchased with cash and from a designated Petty Cash Account. Most NPOs maintain a Petty Cash Account for immediate needs, usually of a small dollar amount. These transactions must meet the adequate documentation requirement and therefore must be accompanied by receipts. Cash transactions on larger items will be harder to document and more likely to be disallowed. (See question 15)

13. Is there a limit to the amount of cash in a “petty cash” account and what types of purchases can be made with petty cash?

No. There is no required limit on a Petty Cash Account. The Board of Directors and senior management should develop a policy that sets the amount of available cash in the Petty Cash Account and a process for how it is to be replenished. It is based on the size and needs of the NPO. If the funds in petty cash are only from AFDC-FC funds then only items that are allowable under the federal grant may be purchased with “petty cash”. Petty cash should not be used as a substitute for normal purchasing and disbursement practices. Petty cash allows the NPO to make small purchases for items such as stamps and office supplies.

14. Do petty cash fund purchases need to be approved?

Yes. The “petty cash custodian” authorizes all petty cash purchases. To maintain adequate internal controls, the petty cash procedures should minimally specify the person responsible for maintenance of the fund (custodian); how the fund is safeguarded (secured/locked/restricted access); the types and amounts of purchases authorized to be made with petty cash; documentation expected for each expenditure; and procedures for disbursement etc.

15. Can cash transactions be done with lump sum withdrawals or checks written to cash, from a bank account?

Generally cash transactions are not advisable. Cash transactions through a petty cash account for small, incidental expenses are allowable with adequate documentation. However, cash bank withdrawals of large amounts outside of the petty cash system are difficult to track and challenging to reconcile.
Cash-based transactions have been disallowed because of the inability to match the receipts with the cash sums withdrawn from a bank account. It is consistent with the goals of internal controls to use debit and credit cards because there is documentation generated to better track expenditures.

Combined with receipts and timely bank statement reconciliation, this affords a better safeguard of NPO assets and avoids risk of error, theft, and disallowance.

16. **Who is ultimately responsible for all purchases, including those made with “petty cash”?**

The Board of Directors remains responsible to ensure that all expenditures made are allowable. While the Board may rely on reports from the Executive Director, accountant, bookkeeper, or other reliable professional, any significant purchases should be reviewed in a Board meeting and documented in Board minutes.

17. **When are dual signatures recommended?**

Dual signatures on business checks are recommended in particular for large purchases. The Board of Directors and executive management should specify the amount over which dual signatures are required.

18. **Why are we required to conduct bank reconciliation when the accountant is already aware of all transactions?**

The Board has ultimate responsibility for the recording and safeguarding of NPO assets. While the Board may reasonably rely upon experts, such as accountants, reconciliation by the NPO Board or delegate(s) is a check and balance to ensure accurate financials. As part of good internal control protocols, timely reconciliation of financial data is crucial for adequate cash-flow management and to maintain accountability for the expenditure of AFDC-FC funds and overall operation of the NPO.

19. **Who issues or signs the payroll checks?**

The Board assigns the payroll responsibility but retains ultimate responsibility for oversight. Payroll may be prepared by the Board (in small NPOs); in house by the Executive Director or a payroll manager; or by an external payroll company.
20. Can the Executive Director sign his/her own payroll check?

No. An essential element of good internal controls is the separation of duties. Allowing an employee, regardless of their status in the organization, to sign and issue their own paycheck, creates the potential for embezzlement and/or fraud because there is a lack of accountability and oversight. The person signing a paycheck should have no personal interest in the money or the person to whom the paycheck is written.

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21. Does the Board have to approve the payroll check for the Executive Director?

No. The Board can assign payroll responsibilities to management, staff, or an outside company. However, the Board retains ultimate responsibility for oversight. If the Board retains payroll responsibility then there must be a quorum of disinterested Board members (e.g. one with no familial, contractual, or other outside business relationships) to approve any payroll or reimbursement. If the Board has assigned payroll responsibility to the Executive Director, the Board may assign someone else, including a disinterested Board member, to issue the Executive’s payroll check.

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22. What if a Board member is paid or reimbursed? Who issues the check?

If a Board member is paid or reimbursed for mileage or out-of-pocket expenses, then a disinterested manager, bookkeeper, or an outside accounting or payroll company should issue the check.

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23. Is there a compensation limit for the Executive Staff?

(2 CFR §200.430; 2 CFR §230, App. B Cost Item 8; Internal Revenue Code §4958)

No. The standard is what is considered “reasonable” compensation. Executive compensation will be considered reasonable to the extent that it is comparable to that paid for similar work in the labor markets in which the organization competes for the kind of employees involved. Consideration is given to the size and income of the NPO, funding of the program, and assets; and whether or not the compensation for its executive staff is reasonable in comparison to similarly situated NPOs. NPOs can look to the reasonableness standards and criteria for executive compensation contained in Internal Revenue Code section 4958 or it may use another outside reliable source to determine what reasonable compensation is.
FCARB uses the Child Welfare League of America salary study to assess reasonableness of salaries. There are other resources available to NPOs both free and for a fee: Charity Navigator 2014; Guidestar; Abbot, Langor; Nonprofit Times; and the IRS 990 instructions.

24. **What is compensation?**

Compensation includes, but is not limited to, salaries, wages, director and executive committee member fees, incentive awards, fringe benefits, personal automobile allowances, pension plan costs, allowances for off-site pay, incentive pay, location allowances, hardship pay, and cost-of-living differentials. The whole package needs to be considered in assessing whether it is reasonable compensation.

25. **What is the difference between allowable, unallowable and unsupported costs?**
(2 CFR §200.403; 2 CFR §230, App. A General Principles, A. Basic Considerations)

An **allowable cost** is one that meets all of the following criteria:

- **Reasonable**: a prudent person would have purchased the item and paid this price. It is recognized as ordinary and necessary.
- **Allocable**: the cost can be assigned to the activity on some reasonable basis.
- **Consistently treated**: Like costs must be treated the same in like circumstances.
- **Be consistent with policies and procedures and are applied uniformly to both federally-financed activities and other activities of the NPO.**
- **Conforms to any limitations or exclusions set forth in the cost principles of the award, in our situation, the expenditure of AFDC-FC funds.**
- **Necessary**: to the overall operation of the organization and or award.
- **Is adequately documented.**

**Unallowable costs** are those that either do not meet the above criteria or are expressly not covered by the grant regardless of the documentation or consistent treatment, e.g. alcohol, personal use of vehicles, lobbying.

**Unsupported costs** are those that lack any or sufficient documentation to verify that they are allowable consistent with the above criteria.
26. Are there special requirements for capital expenditures? And what are capital expenditures? (2 CFR § 200.439)

Yes. Capital expenditures must meet pre-authorization requirements. Capital expenditures are expenditures to acquire capital assets or expenditures to make additions, improvements, modifications, replacements, rearrangements, reinstallations, renovations, or alterations to capital assets that materially increase their value or useful life. The federal regulations contain specific requirements depending on whether the expenditures are treated as direct or indirect charges. For example, capital expenditures for general purpose equipment, buildings, and land are unallowable as direct charges, except with prior written approval by CDSS. Capital expenditures for special purpose equipment are allowable as direct costs, provided that items with a unit cost of $5,000 or more have prior written approval from CDSS.

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27. Can the NPO obtain pre-approval/pre-authorization from the State when it is uncertain about the allow-ability of a special or unusual cost?

Yes. If the NPO is uncertain whether a cost is allowable, it may consult with its Rate Analyst in advance of the incurrence of the special or unusual cost.

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28. Can the NPO purchase a vehicle?

Yes. It is the responsibility of the Board of Directors to review for business necessity and reasonableness, and approve all major purchases made by the NPO. Automobiles are categorized as “general purpose equipment”, the purchase or lease of which require pre-approval where the cost will exceed $5,000.00. Advance approval for a generic automobile for an allowable purpose will not ensure allow-ability if it is not also reasonable and for the benefit of the children in care. In addition, any cost associated with the personal use of the vehicle is not an allowable cost. (See question 32)

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29. What type of documentation must be maintained to support the allow-ability of an acquisition or lease of a vehicle?

The NPO should minimally have available the following:

- Pre-approval obtained from CDSS for the purchase or lease of the vehicle where the cost will exceed $5,000.00.
- General ledger associated with the vehicle or vehicles.
- Purchase/sales agreements, finance agreements, lease agreement, contracts, insurance records, invoices, mileage logs, credit statements, cancelled checks, and bank statements associated with the vehicle.
• Board approval that reflects it has considered the transaction to be reasonable, necessary and for the benefit of the purpose of the NPO and the children that it serves.

  Note: the auditors will look to determine whether the Board has considered the initial expense, ongoing costs, final cost, and types of usage (total business miles versus personal miles) prior to determining if the purchase or lease is a reasonable cost to incur.

• After purchase, the NPO must maintain purchase/lease agreements, mileage logs, and maintenance records. It is very important that mileage logs reflect a business purpose for each trip, starting & ending address, and mileage for each trip. It is necessary to have a log to ensure that there is no unauthorized use.

30. Can the Board assign NPO-purchased or leased automobiles to staff?

Yes. Assuming the purchase or lease of the vehicles otherwise meets the requirements for allow-ability; the Board may assign a vehicle to staff as needed for the business purposes of the NPO. If there is dual use, for business and personal (such as commuting) then the mileage cost of the automobile must be allocated accordingly. For example, auditors will look for mileage logs that document and allocate the business versus personal use.

31. The group home requires 24/7 care and the Executive/Administrative staff are on call 24/7. Do we still need to keep mileage logs when everything we do is childcare related?

Yes. That portion of the cost of organization-furnished automobiles that relates to personal use (including transportation to and from work) is unallowable as a fringe benefit or indirect costs regardless of whether the cost is reported as taxable income to the employees. Mileage logs are required to support the business purpose of the usage of NPO vehicles or personal vehicles used on behalf of the NPO. Commuter miles will not be allowed.

32. Why was the NPO’s purchase of a Mercedes or Escalade that was assigned to an executive staff member, disallowed when it was exclusively used for business purposes of the NPO?

The auditors will review all expenditures to determine whether they meet the reasonable and necessary standards required for an allowable cost.
Auditors expect that the Board will have reviewed and approved the purchase or lease of a vehicle to determine that it meets these standards.

There are some make or models of vehicles that the auditors will scrutinize for the use of and ultimate cost to the NPO in comparison to other alternatives. For example, the purchase of a vehicle that ultimately costs the NPO $100,000.00; or the lease of a high-end vehicle costing the NPO $1,200.00 a month, will be assessed in light of prudent and reasonable alternatives. The auditors will assess whether the Board evaluated the expenditure, considered alternatives and will review whether and the extent to which, the vehicle is being used for personal rather than business purposes; and whether children are benefitting from the vehicle or if it really is only being used by an executive staff member as a luxury being paid with AFDC-FC funds.

If the auditors determine the expenditure to be unallowable the entire purchase will be disallowed.

33. The vehicle assigned to the Executive Director needs repairs. Can s/he get a rental car?

Yes, if the vehicle is owned by the NPO and used exclusively for NPO business-related activities. However, the rental cost must still be reviewed by the auditors for documentation to determine if the cost of the rental car was reasonable, necessary and benefited the children in the program. Auditors will review all documentation provided to support the cost including but not limited to the general ledger, credit card statements or cancelled check, invoices, original, annotated receipts, availability of other company vehicles, mileage logs, and business purpose of the trips taken with the rental car.

34. Can the NPO use AFDC funds to pay for penalties issued by the federal, state, and/or county agencies?

No. Fines and penalties resulting from violations of or failure of the organization to comply with federal, state, and local laws and regulations are unallowable except when incurred as a result of compliance with specific provisions of an award or instructions in writing from the awarding agency.

35. Can staff, administrative or line, attend industry-related conferences/seminars (in state and out-of-state)? What type of documentation is needed to support the costs?
Yes staff can attend the conference, seminar or similar event if it is reasonable and necessary for the successful performance of the federal award.

The NPO must at a minimum maintain course advertisement, agendas, course material, credit card statements or cancelled check, original receipts, and invoices. The costs of travel directly related to attendance to an industry related seminar are also allowable provided that the costs are reasonable and necessary. The NPO should make every effort to enroll its staff in seminars held locally or within the State of California. Out of state travel will be scrutinized for reasonableness and necessity in light of alternative industry-related, more cost effective and appropriate seminars within the State of California.

However, cost of entertainment, including amusement, diversion, and social activities and any costs directly associated with such costs (such as tickets to shows or sports events, meals, lodging, rentals, transportation, and gratuities) are unallowable.

NOTE: If the NPO is sponsoring a conference, allowable conference costs paid by the non-federal entity as a sponsor or host of the conference may include rental of facilities, speakers’ fees, costs of meals and refreshments, local transportation, and other items incidental to such conferences. 2 CFR §200.432 clarifies allowable conference spending and requires conference hosts/sponsors to exercise discretion and judgment in ensuring that conference costs are appropriate, necessary and managed in a manner that minimizes costs to the federal award. Additionally, the costs of identifying (but not providing) locally available child-care resources are allowable.

36. If the NPO has a credit card account and/or line of credit to meet the daily needs of the NPO, and interest charges are part of the credit card contract, are the interest payments allowable? (2 CFR §200.449; 2 CFR §230, App. B, Cost Item 23)

No. The Board and its Executive team have been given the fiduciary responsibility to secure and manage the NPO’s assets and manage expenditures made with AFDC-FC federal funding. Interest may be avoided by timely payment of the outstanding credit card balance.

As stated before, interest costs incurred on borrowed capital are unallowable except for financing costs to acquire, construct, or replace capital assets subject to conditions.

The NPO can choose to use alternative sources of funding for these costs, but in doing so, must be able to verify through adequate documentation, that alternative funds were used.
37. Are bank fees allowable?

Yes. Bank fees that are inherent to the maintenance of a particular account are allowable. However, fines and penalties such as overdraft fees, insufficient fund fees, and late fees are not allowable costs.

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38. If the Staff members are using their personal vehicles for business purposes, can the NPO reimburse them for the repairs to their personal vehicles?

Yes. However, it must be consistent with the IRS "actual expense method". The employee must determine actual costs to operate the car for the portion of the overall use of the car that is business use. Include gas, oil, repairs, tires, insurance, registration fees, licenses, and depreciation (or lease payments) attributable to the portion of the total miles driven that are business miles. See IRS publication 510 on this subject. There are many specific requirements including when the reimbursement to the employee is taxable and when it is not. It is advisable to consult with the NPO accountant if this method is going to be used rather than a mileage reimbursement system.

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39. Can the NPO hire a handyman to perform routine repairs and maintenance to the facility?

Yes, if the expenditure is otherwise allowable and to the extent not paid through rental or other agreements. Costs incurred for utilities, insurance, security, necessary maintenance, janitorial services, repair, or upkeep of buildings and equipment that do not add to the permanent value of the property or appreciably prolong its intended life, but keep it in an efficient operating condition, are allowable. Costs incurred for improvements, which add to the permanent value of the buildings and equipment or appreciably prolong their intended life must be treated as unallowable capital expenditures unless prior approval from FCARB has been obtained.

The NPO should first review the lease agreement to determine who is responsible for the repairs and maintenance of the leased facility. In general, it is unreasonable to expect the lessee to pay for the costs of repairs and maintenance of a leased facility unless the need for the repairs and maintenance arises from damages caused by the NPO’s clients.
If the property lease provides that it is the responsibility of the NPO to perform routine repairs and maintenance to the facility, the NPO may hire a handyman assuming compliance with otherwise required laws associated with the use of handymen services in the California Business and Professions Code.

At the time of this publication, an exemption from licensure for minor work is made if the aggregate contract price, including labor, materials, etc. is less than $500. (Cal. Bus. & Prof. Code §7048 (Small Operations)). This exemption does not apply if the "minor work" is part of a larger project. Example: A homeowner is having a kitchen remodeled at a total cost of $6,000 and decides to sublet the flooring work, which is only $300. The person doing the flooring would not be exempt from licensure because the overall cost of the project was over $500. In addition, jobs cannot be broken down into hourly fees in order to sidestep the $500 threshold.

40. Are hand-written receipts for these routine repairs acceptable as supporting documentation?

Yes. The NPO should, at a minimum, maintain original receipts, invoices with the identity, address, and phone number of the handyman, original bids, detailed description of the services rendered, and canceled check. Cash payments for repairs and maintenance services should be avoided because they do not safeguard assets, and checks will provide better documentation of the expenditure and business purpose.

It is generally more prudent to engage the services of a licensed contractor who can provide warranties for services rendered and assure the health and safety of the children and placement.

41. Can we throw a holiday party for our staff and children? Can we take our staff and children for dinner for special occasions? (2 CFR §200.438; 2 CFR §230, App. B, Cost Item 14)

Yes, if conditions are met. Costs of entertainment, including amusement, diversion, and social activities and any associated costs are unallowable, except where specific costs that might otherwise be considered entertainment have a **programmatic purpose** and are **authorized** either in the **approved budget** for the Federal award or with **prior written approval** of the Federal awarding agency, FCARB. All costs must still be reasonable and adequately documented and otherwise meet requirements to be allowable. As with any expenditure, the NPO should maintain, at minimum, original itemized receipts, invoices, contract agreement, cancelled checks, and list of attendees.
Note: A dinner or activity for staff may be allowable pursuant to 2 CFR 200.437 if it improves working conditions, employer-employee relations, employee health, or employee performance, the NPO has a written policy, and the costs are otherwise reasonable and necessary to the NPO business purpose.

42. We would like to purchase special door prizes such as IPADS, Nooks, etc. for an approved holiday party. What type of documentation is needed to justify the costs?

Allowable, if conditions are met. The Board may authorize holiday parties for staff and children if it determines that there is a valid programmatic purpose and it has prior approval. Costs of entertainment, including amusement, diversion, and social activities and any associated costs are unallowable, except where specific costs that might otherwise be considered entertainment have a programmatic purpose and are authorized either in the approved budget for the Federal award or with prior written approval of the Federal awarding agency, FCARB.

All costs must still be reasonable and adequately documented and otherwise meet requirements to be allowable. As with any expenditure, the NPO should maintain, at minimum, original itemized receipts, invoices, contract agreement, cancelled checks, and sign-in sheets of attendees, and signatures of the recipients of the door prizes certifying that they received the gift, with a description of the gift received. All requests must include the proposed distribution process and protocol that will be followed to ensure all gifts are only distributed to allowable clients, and not to employees.

Note: Prizes for staff may be allowable pursuant to 2 CFR 200.437 if it improves working conditions, employer-employee relations, employee health, or employee performance, the NPO has a written policy, and the costs are otherwise reasonable and necessary to the NPO business purpose.
43. The NPO took the children to a well-known amusement park in California for an outing. Is this an allowable cost? If yes, what type of documentation is required for reimbursement?

Yes, if the outing met the requirements of 2 CFR 200.438. As discussed above, entertainment costs are generally unallowable. However they are allowable if they have a programmatic purpose and are pre-authorized by FCARB or are a part of an approved budget. Child related entertainment costs will be evaluated against the backdrop of the intended purposes of Title IV-E care of foster children. The auditors will review any children-related entertainment costs to ensure that they are reasonable, necessary, fairly distributed, adequately documented and have a programmatic purpose. The review process will include, but not be limited to, the review of original receipts, cancelled checks, ticket stubs, Board approval, or FCARB approval if necessary, for the expense, daily logs, and interviews of the Board members and the children in placement. Note that staff presence necessary for the care and supervision of the children during the outing or that has another valid programmatic purpose is allowable if the outing otherwise meets the above purposes.

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44. The NPO took the children and staff on an overnight trip to San Francisco to tour the city and its sights. Some of the vendors such as the Alcatraz Tours do not provide receipts. How can the NPO prove that the children went to San Francisco when they are no longer in placement?

Costs not documented by receipts or other form of documentation will be disallowed. Cash transactions without receipts will be disallowed. CDSS suggests that the NPO maintain a contemporaneous record of the trip specifying expenditures and paying with either checks or credit cards that can support the expenditures. Retention of boarding tickets, contemporaneously taken pictures, will help to support that the trip did take place. However, there must be some form of verification of the actual costs.

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45. Can the NPO sign a contract for outside services if a member of the Executive Staff and/or Board owns the company?

Yes, if the Board complied with the requirements of the Cal. Corp. Code §5233. Compliance must be established through Board minutes and/or resolution and appropriate documentation in support of the decision. The Board of Directors may approve a self-dealing transaction with a majority vote of the directors then in office, excluding the vote of all interested parties. This approval should be given only if the terms of the contract are fair and reasonable to the NPO, the contract is for the NPO’s benefit (not the Board member’s benefit), the NPO could not have obtained a better arrangement with reasonable effort, and there is not likely to be any damage to the corporation from the self-dealing transaction.
46. If children would benefit from having a recreation room in the group home, can we use AFDC-FC funds to convert the garage?

Prior to considering any changes to any building, land, or equipment, the NPO must first review its lease agreement to determine if improvements are authorized and to identify which party is responsible for the costs of such improvements. The Board of Directors must also approve any improvements. The NPO must also consider that such expenditures will require pre-approval from FCARB if they constitute capital expenditures.

47. One of the children broke the kitchen countertop. Since it needs to be repaired, can the NPO upgrade the countertops to granite since it will be more durable?

(2 CFR §§200.439 and .452)

The NPO should first review all applicable lease agreements to identify the party responsible for repairs and maintenance of the property. It is likely that the NPO will be responsible for the repair as the NPO client caused the damage. In that case, any repair should bring the countertop back to its original condition. The Board may explore other more durable materials that do not increase the cost to the NPO’s federal grant or the value of the property.

Costs incurred for necessary maintenance, repair, or upkeep of buildings and equipment that keep it in an efficient operating condition, which neither add to the permanent value of the property nor appreciably prolong its intended life, are allowable.

If the granite countertops add permanent value to the property, such upgrades would be deemed a capital improvement and disallowed. Capital expenditures for improvements to land, buildings, or equipment, which materially increase their value or useful life, are unallowable as a direct cost except with prior written approval from FCARB.

48. Can AFDC-FC funds be used to pay for professional memberships, subscriptions?

(2 CFR §230, App. B, Cost Item, 14; See also 2 CFR §200.454)

Yes. Generally costs for subscriptions to business, professional, and technical periodicals are allowable. Costs for memberships in business, technical and professional organizations are allowable. Costs of membership in any civic or community organization are allowable with prior approval from FCARB. However, costs of membership in any country club or social or dining club or organization are unallowable. Costs of membership in lobbying organizations are unallowable.
49. Can AFDC-FC and other funds be commingled? The NPO operates other related programs with different sources of funding. The NPO also organizes a yearly fund-raiser to help defray the costs of running a group home. Since all the money raised is used to benefit the children, can we deposit the money in the same account as the AFDC-FC funds?

The funds must be separately identifiable and traceable either physically or by a designated accounting method. The clearest way to separate funding sources is that the NPO maintain a separate account for different funding sources. However, if the NPO decides to deposit money from other sources into the same account as AFDC-FC funds, the funds for each source of revenue and expenditure must be clearly identified and traceable in the accounting records.

Identification of AFDC-FC and non-AFDC-FC funds and expenses is particularly important if the NPO relies on the “other” funds to cover expenditures that are unallowable uses of AFDC-FC funds. However, if account coding is used to identify and segregate revenue and expenditures, it is imperative that the NPO be able to generate a report or similar documentation to show the source and specific use of funding. The account activity must support proper use of the federal funding.

50. Can the NPO use AFDC-FC funds to donate to a cause related to their program?
(2 CFR §200.434(a); 2 CFR §230, App. B, Items of costs 12)

No. Costs of contributions and donations, including cash, property, and services, from the non-Federal entity to other entities, are unallowable. However, donations can be made from “other sources” if properly documented support is maintained.

51. Is there a limit to rental/lease costs?
(2 CFR §200.465(a); 2 CFR §230, App. B, Cost Item 43)

Yes. Lease costs are limited to fair market rental value (FMRV). Rental costs are allowable to the extent that the rates are reasonable in light of such factors as: rental costs of comparable property, market conditions in the area; alternatives available and the type, life expectancy, condition, and value of the property leased. (Note CDSS regulation MPP §11-402.825(i) allows reimbursement for the cost of one appraisal per year per facility.)
52. What is a “self-dealing” or “less-than-arm’s-length transaction”? Is there a difference?

Yes there is a difference. The Cal. Corp. Code §5233 defines a “self-dealing” transaction as a “transaction to which the corporation is a party and in which one or more of its directors has a material financial interest...” Cal. Corp. Code §5227 defines “interested persons” as it relates to influence and self-dealing transactions as either a person being compensated by the NPO currently or within the previous 12 months; or any brother, sister, ancestor, descendant, spouse, brother-in-law, sister-in-law, son-in-law, daughter-in-law, mother-in-law, or father-in-law of any such person.

The federal regulations 2 CFR §200.465(c) describes a “less-than-arm’s-length transaction” as one under which one party to the lease agreement is able to control or substantially influence the actions of the other.

The federal law is more expansive than California law in its definition of whom or what may have substantial influence in a transaction. These include transactions between: “(1) Divisions of the [NPO]; (2) The [NPO] under common control through common officers, directors, or members; and (3) The [NPO] and a director, trustee, officer, or key employee of the [NPO] or an immediate family member, either directly or through corporations, trusts, or similar arrangements in which they hold a controlling interest. For example, the [NPO] may establish a separate corporation for the sole purpose of owning property and leasing it back to the [NPO].”

53. Are the requirements the same for “self-dealing” or “less-than-arms-length lease/rental costs?”
(2 CFR §200.465(c)(3); 2 CFR §230, App. B, Item of Costs 43; Welf. & Inst. Code §11462.06(d); Cal. Corp. Code §5233; MPP §11-402.827(1))

No. The requirements differ if the NPO is a group home. The state law does not allow self-dealing transactions involving shelter care (rental costs) by group homes. The group home cannot receive an AFDC-FC rate if it is involved in a self-dealing transaction pursuant to Welf & Inst. Code §11462.06(d).

There are additional requirements under the federal regulations for “less-than-arm’s-length” leases that apply to rental leases to all NPOs that are recipients of federal monies. The “less-than-arms-length” lease is one under which one party to the lease agreement is able to control or substantially influence the actions of the other.
Under the federal regulations this includes, but is not limited to lease arrangements involving the NPO and a director, trustee, officer, key employee of the non-profit organization, spouse, other family members, domestic partners, even individuals related by blood or have a close relationship that is equivalent to a family relationship. It can also include arrangements involving other divisions of the NPO or related corporations, trusts, or similar arrangements in which one holds a controlling interest over the NPO. (2 CFR §200.465 (c)).

The “less-than-arm’s-length” lease discussed in 2 CFR §200.465(c) is allowable only up to the amount that it would cost had the NPO held on to the property since the date the property was purchased. The same analysis of the cost of ownership (had the NPO owned rather than leased the property) as in 2 CFR §200.465(b), considers the expenses such as depreciation, maintenance, taxes, and insurance when the property was originally purchased.

There is a similar scenario termed a “sale and lease back” in federal regulations, where the NPO buys a property, sells it, and leases it back to the NPO addressed in 2 CFR §200.465(b). The rental costs under “sale and lease back” arrangements are allowable only up to the amount that would be allowed had the NPO continued to own the property rather than enter into the lease. The analysis of the cost of ownership (continued ownership) considers expenses such as depreciation, maintenance, taxes, and insurance as if the NPO retained ownership of the property. The question is whether the NPO would have had a better deal (and lower cost to the federal grant) had the NPO retained ownership of the property.

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54. What if the lease is for a “residential shelter care cost”? (2 CFR §200.465; 2 CFR §230, App. B, Item of Costs 43; Welf. & Inst. Code § 11462.06; MPP §11-402.827(1))

In a free market (arm’s length) lease, in addition to the federal regulation at 2 CFR §200.465(a), Welf. & Inst. Code § 11462.06(a) is applicable where residential property leased or rented for an NPO group home program is involved. The rental costs cannot exceed 12% of fair market value of the property at the inception of the lease or when the lease is renewed.

If the rental for the NPO group home program is both a residential lease and a “less-than-arms-length” transaction, notwithstanding the federal regulation at 2 CFR §200.465(c), subdivision (d) of Welf. & Inst. Code § 11462.06 prohibits payment of an AFDC-FC rate at all whenever there is a self-dealing lease. [Back to Q&As]
55. What type of documentation is required for lease agreements?

NPOs should retain appraisals, evidence of comparable property or equipment, property tax statements, lease agreements, and any other documentation to assist the auditors to determine reasonableness of rental costs.

Auditors will minimally request the following records:

- Lease agreements;
- Purchase price, property value for land and improvements, date of purchase, and interest rate;
- Owner’s annual depreciation for each property to support how depreciation was calculated. For example, documentation that includes the property values for land and improvements, the date of purchase, depreciation basis etc.;
- Annual interest payments such as the IRS form 1098 Mortgage Interest Statement;
- Annual Property Tax statements;
- Annual Property Insurance statements or invoices;
- Annual Property Maintenance records and Costs Worksheet; and
- Documentation of Board of Directors’ approval for rental costs of real property and equipment including documentation the Board has assessed the reasonableness of the transaction.

56. What happens if we are not using the entire facility leased for our group home; or one of our group homes (three in the program) is not being used at all? Is there an impact on the allowability of the rent/lease?


Per the federal regulations, an idle facility includes completely unused land and buildings, that are in excess of the current needs of the NPO; the rent/lease for which is entirely unallowable. However, federal law allows for exceptions when (1) it is necessary to retain the idle facility to accommodate foreseeable fluctuation in placement; or (2) if not necessary for fluctuation, then the use of the facility was necessary when acquired and is now idle because of changes in program requirements, efforts to achieve more economical operations, reorganization, termination, or other causes which could not have been reasonably foreseen.” Even with this exception, costs of idle facilities are allowable only for a “reasonable period of time.” The period depends on the action of the NPO to mitigate the cost by use, lease or disposition; ordinarily not more than one year.

Idle capacity means partially used facilities. Idle capacity is usually allowable to the extent that the idle capacity is the result of fluctuation that is a reasonably
foreseeable cost of doing business; and mitigation by sublet, rent, sale, etc. is not feasible. However, if the idle capacity is widespread, it can be treated as an idle facility noted above and disallowed. If a part of the lease is disallowed based on idle capacity the amount disallowable is the difference between the intended maximum use and the actual use of the facility.

Disallowance based on idle facility/capacity includes the costs of maintenance, repair, housing, rent, and other related costs, e.g., insurance, interest, and depreciation.

57. Can AFDC-FC funds be used for cash gifts/gift cards/bonuses/other incentives to boost employee morale?
(2 CFR §200.437; 2 CFR §230, App. B, item of cost 8(j))

Costs incurred in accordance with the NPO's documented policies for the improvement of working conditions, employer-employee relations, employee health, and employee performance are allowable. Such costs are allowable to the extent that they are found to be reasonable, paid or accrued pursuant to a pre-approved written agreement entered into in good faith between the NPO and the employees before the services were rendered, or pursuant to an established plan followed by the NPO that is so consistent as to imply, in effect, an agreement to make such payment.

It is up to the Board of Directors to determine and approve if bonuses or other forms of compensation are reasonable and warranted. The Board of Directors must first establish and approve a reasonable, measurable plan prior to the issuance of any such gifts/bonuses/ incentives. The NPO should maintain, at minimum, Board minutes, bonus policy, original receipts, invoices, ticket stubs, gift card numbers, and signatures of the recipients, proof of efficient performance, and any other documentation that may substantiate the transaction.

58. Can a Board member hold different offices at the same time?
(Cal. Corp. Code §5213(a))

Yes. California Corporation Code 5213(a) states “any number of offices may be held by the same person unless the articles or bylaws provide otherwise, except that the secretary, the treasurer, or the chief financial officer may not serve concurrently as the president or chair of the board.”

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59. Can the members of the Board be held responsible for the wrongdoings of an Executive Director and/or staff if they were not aware of the wrongful actions?

Yes. NPOs are not “owned” by anyone but rather governed by the Board. The members of the Board are responsible for establishing the policies of the NPO while the Executive team manages the day-to-day operation of the organization. However, as the governing body, the Board is ultimately responsible for the direction and affairs of the organization. The members of the Board have a fiduciary responsibility and ultimately, a legal responsibility for the actions, or lack thereof, taken by the organization as a whole. The members of the Board are expected and required to act reasonably, and in the best interest of the organization in order to avoid negligence, fraud, and conflict of interests. See also Questions #65 and #70 below.

60. Can the members of the Board be compensated for their services?  
(Cal. Corp. Code §5227(b)(1))

Yes. California law allows board members to receive “reasonable compensation.” However, this is not standard practice within the nonprofit community. National charitable standards state that board members should be volunteers with occasional reimbursement for actual expenses for meetings and conferences that are directly related to the activities of the NPO. The auditors will need documentation to support the validity of Board member compensation.

However, there cannot be more than 49 percent “interested directors” serving on the Board. An interested director is one who is or has been a paid employee or contractor within the last year. The “49%” rule has to do with employees/contractors and specifically excludes “reasonable” compensation made to a director. Cal. Corp Code §5227 in pertinent part provides:

"Not more than 49 percent of the persons serving on the board of any corporation may be interested persons. (...) For the purpose of this section, "interested persons" means either: Any person currently being compensated by the corporation for services rendered to it within the previous 12 months, whether as a full- or part-time employee, independent contractor, or otherwise, excluding any reasonable compensation paid to a director as director." Emphasis added.

It is strongly recommended that interested directors be kept at a minimum in order to uphold the best interest of the corporation, minimize the likelihood of self-dealing transactions, and so as not to confuse the issues of authority and supervision.
61. Can family members serve on the Board at the same time?  
(Cal. Corp. Code §5227(b)(2))

Yes. However, it is discouraged. It is not always in the NPO’s best interest to have family members serve simultaneously, because these individuals are “interested persons.” There will be built-in conflict if related individuals serve simultaneously.

The Cal. Corp. Code states in pertinent part that not more than 49 percent of the persons serving on the board may be interested persons. The Cal. Corp. Code defines interested person as, “… Any brother, sister, ancestor, descendant, spouse, brother-in-law, sister-in-law, son-in-law, daughter-in-law, mother-in-law, or father-in-law of any such person.”

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62. What is a quorum?  
(Cal. Corp. Code §5211(a)(7))

The California Corporations Code defines a quorum as follows: “A majority of the number of directors authorized in or pursuant to the articles or bylaws constitutes a quorum of the board for the transaction of business. The articles or bylaws may require the presence of one or more specified directors in order to constitute a quorum of the board to transact business, as long as the death or nonexistence of a specified director or the death or nonexistence of the person or persons otherwise authorized to appoint or designate that director does not prevent the corporation from transacting business in the normal course of events. The articles or bylaws may not provide that a quorum shall be less than one-fifth the number of directors authorized in or pursuant to the articles or bylaws, or less than two, whichever is larger, unless the number of directors authorized in or pursuant to the articles or bylaws is one, in which case one director constitutes a quorum.”

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63. What is the definition of an “interested party?”  
(Cal. Corp. Code §5227)

Cal. Corp. Code §5227 defines “interested party” as follows: “(b)(1) any person currently being compensated by the corporation for services rendered to it within the previous 12 months, whether as a full- or part-time employee, independent contractor, or otherwise, excluding any reasonable compensation paid to a director as a director; or (b)(2) any brother, sister, ancestor, descendant, spouse, brother-in-law, sister-in-law, son-in-law, daughter-in-law, mother-in-law, or father-in-law of any such person.”

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64. How often is the Board supposed to meet?
   (Health & Safety Code §1520.1(e); Cal. Corp. Code §§5510 - 5527)

   Health and Safety Code Section 1520.1(e) requires that meetings be held at least every three (3) months. General provision for meeting and voting found in Cal. Corp. Code Chapter 5. Meetings and Voting §§5510 - 5527.

65. What are the responsibilities of each Board Member?
   (Cal. Corp. Code §§5210 - 5260)

   In general, the members of the Board of Directors act as the trustees of the NPO’s assets, and are therefore responsible for ensuring that the NPO remains fiscally sound. They establish the policies of the NPO, provide oversight of the overall program operations, and ensure that all transactions entered into are in the best interest of the NPO. They are expected to actively participate in and approve the NPO’s long term goals and directions, monitor the NPO’s budget and major purchases, protect the NPO’s assets, and comply with all applicable federal, state and local laws and regulations. More specific and additional duties are based on the specific role/position taken as a member of the Board of Directors. See Cal. Corp. Code §§5210-5260 for Board duties.

66. Can the NPO lease a commercial facility from the Executive Director or a Board Member; and how is fair market rent determined?
   (2 CFR §200.465(c))

   Yes. However, the lease transaction would still be subject to evaluation under 2 CFR §200.465(c), which contains limitations on rental costs that are “less-than-arms-length” leases. The cost of ownership would be established in the same manner as a “sale and lease back” in 2 CFR 2 CFR §200.465(b). See discussion above on Rental Costs of Buildings.

67. Can the NPO lease a residential facility from the Executive Director or a Board Member; and how is fair market rent determined?
   (2 CFR §200.465(c); Welf. & Inst. Code §11462.06(d); Cal. Corp. Code §5233)

   No, Welf. & Inst. Code §11462.06(d) prohibits a self-dealing shelter care/residential lease transaction as defined in Cal. Corp. Code §5233. The Board Member would have to step off of the Board. However, even if the Lessor is no longer a Board member, the lease transaction would still be subject to evaluation under 2 CFR §200.465(c), which contains limitations on rental costs that are under “less-than-arms-length” leases.
Less-than-arm’s-length leases include arrangements involving the NPO and a
director, trustee, officer, key employee of the non-profit organization, spouse,
other family members, domestic partners, even individuals related by blood or
have a close relationship that is equivalent to a family relationship. It can also
include arrangements involving other divisions of the NPO or related
corporations, trusts, or similar arrangements in which one holds a controlling
interest over the NPO.

Another consideration is that a “shelter care” cost/ residential lease can be no
more than the lesser of 2 CFR §200.465(c) (cost of ownership analysis) or Welf.
& Inst. Code §11462.06(a), 12% of fair market value.

68. Can the auditors consider overall success of the program and or the
happiness and success of the children in placement to mitigate any
disallowed costs/findings?

No. The CDSS auditors are always glad to see that children in placement are
thriving and gaining life experiences consistent with the intentions of the
AFDC-FC program. Fiscal audits, however, are based on legally specified
funding requirements. The auditors are required to apply all the Federal and
State laws and regulations that govern fiscal accountability from entities receiving
federal funding.

69. How does the payment plan work? Who do we contact to discuss a
payment plan?
(Welf. & Inst. Code, §11466.25)

The NPO may be given an opportunity to repay the disallowed cost through an
installment plan approved by the CDSS. Please note, however that interest will
begin to accrue on a provider’s overpayment from the date of issuance of the
Final Management Decision Letter. Our Collections Auditor will contact the NPO
to discuss a potential payment plan at the appropriate time.

70. Are the Board members and/or Executive Staff personally responsible to
reimburse the State for any overpayments that result from a fiscal audit?
(Cal. Corp. Code §5230, 5231, 5233)

No. The members of the Board of Directors and/or Executive team are generally
not held personally liable so long as they carry out their duties in good faith, in a
manner believed to be in the best interests of the NPO, with care and reasonable
inquiry, as an ordinary prudent person in like position and similar circumstances.
The Board members may rely on information, opinions, reports or statements, including financial statements in the conduct of their duties presented by those believed to have the requisite knowledge and competence. This includes reasonable inquiry and reliance upon others related to any overpayments.

A notable exception is where the Board member is involved in a self-dealing transaction under Cal. Corp. Code 5233.

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71. We have been in business for quite some time and have never been audited. Why now? (MPP §11-402.51)

The Department has the authority to conduct several types of audits, including fiscal. Fiscal audits are based on referrals or random selection. Referrals can be triggered in numerous ways including complaints, questions raised in a Financial Audit Report, or licensing concerns.

Auditors are required to apply all the state and federal laws and regulations that govern the group home or foster family agency equitably once the NPO is selected for an audit.

MPP §11-402.51 states, in part, “The Department shall conduct a full or partial program or fiscal audits of any program(s), as often as necessary, to ensure compliance with all requirements within this section.”

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72. Can the NPO use AFDC-FC funds to repay the disallowed costs that result from a fiscal audit?

Yes. The NPO may pay a portion from its administrative reimbursement, so long as it does not interfere with the administration of services to children.

Both an FFA and a GH have an administrative portion to the AFDC-FC rate. The FFA rate specifically identifies the administrative portion; while the GH rate RCL system was developed considering the administrative portion that would be paid from the rate. Each can repay from the AFDC-FC rate, but cannot pay from the portion of the AFDC-FC rate that is for the “foster care maintenance payment” for the care and supervision of the children in care.

The FFA would pay from the identified administrative portion. The GH would pay 3% or 5% of their rate, depending on whether voluntary or involuntary payments are made, pursuant to Welf. & Inst. Code §11466.22(d)(3) or (4) respectively. Or a Provider could pay the overpayment from an alternate source or donation.
If paid from an alternate source, that source must be identified and the NPO must be able to document that the expenditure was indeed paid from that alternate source.

73. Can the NPO rate be terminated or its licensed revoked because of audit findings?
(Health & Safety Code §1550 (f); MPP §§11-405.234 and 11-402.393)

Yes. However, generally audits lead to successful corrective actions, payment of overpayments and are not cause for further administrative actions. Audits that raise questions about financial malfeasance can result in rate termination actions or licensing revocation actions.

MPP §11-405.234(a) states, “Pursuant to Section 11-402.393, The Department may terminate the rate of a non-profit corporation that is found to have committed misuse or fraud including, but not limited to, the following circumstances:

1) Multiple occurrences of misuse; or
2) Failure to pay on amounts determined by the Department to be misuse or fraud; or
3) An office or director of a non-profit corporation is convicted of fraud, embezzlement, deception, theft and/or material misrepresentation regarding the corporation’s operation of its group home or foster family agency program.”

MPP §11-405.234(b) further states, “Pursuant to Section 11-402.393, the Department may terminate the rate of a non-profit corporation that has failed to substantially comply with expected corrective actions as specified in a Management Decision Letter.”

A license may be revoked if the licensee has engaged in acts of financial malfeasance concerning the operation of a facility or certified family home, including, but not limited to, improper use or embezzlement of client moneys and property or fraudulent appropriation for personal gain of facility moneys and property, or willful or negligent failure to provide services. (Health & Safety Code §1550 (f)).
Relevant Federal and State Laws, Regulations and Guidance

U.S. Office of Management and Budgets (OMB) Publications
For the most current information that includes changes or updates to the OMB circulars, go to the Office of Management and Budget website at:
http://www.whitehouse.gov/omb/circulars_default/

Code of Federal Regulations (CFR)

2 CFR 230
2 CFR 200
2 CFR 200 federal register:

Audit Standards

Single Audit Process

Generally Accepted Auditing Standards (GAAP) 2 CFR 200.249
FASB http://www.fasb.org/home

Government Auditing Standards (Yellow Book)
http://www.gao.gov/govaud/ybk01.htm

Standards for Internal Control for the Federal Government (Green Book)
http://www.gao.gov/greenbook/overview

California State Statutes

California Corporations Code §§5210 through 5260.
http://leginfo.legislature.ca.gov/faces/codes_displayexpandedbranch.xhtml

Welfare and Institutions Code Sections 11466 et. seq.
CDSS Manual of Policies and Procedures (MPP) – Foster Care

MPP Section 11-400 through 11-401.5: (Definitions/Family Home Rates)

MPP Section 11-402.1 through 11-402.431(c)(2): (Group Home Rate Setting)
www.dss.ca.gov/getinfo/pdf/fcmanb.pdf

MPP Section 11-402.431(d) through Section 11-402.944: (Group Home Rate Setting)
www.dss.ca.gov/getinfo/pdf/fcmanc.pdf

MPP Section 11-403(a) through Section 11-430.361: (403-Foster Family Agency Rates,
405-Fiscal and Financial Audits, 430-Foster Care Administrative Review Procedures)
www.dss.ca.gov/getinfo/pdf/fcmand.pdf

MPP Section 11-430.4 through Section 11-430.74: (430-FC Admin. Review Procedures)
www.dss.ca.gov/getinfo/pdf/fcmane.pdf

Foster Care Audits and Rates Letters (FCARL)

FCARL No. 2004-02 - Financial Audit Requirements
www.cdss.ca.gov/getinfo/fcarl04/pdf/fcarl04_02.pdf

FCARL No. 2005-02 - Financial Audit Requirements, Issues, and Updates
http://www.dss.ca.gov/getinfo/fcarl05/PDF/fcarl05_02.pdf

FCARL No. 2006-04 - Aid to Families with Dependent Children-Foster Care (AFDC-FC) Rates for Group Homes-Program Information
http://www.dss.ca.gov/getinfo/fcarl06/PDF/fcarl06_04.pdf

FCARL No. 2009-01 - Assembly Bill X4 4 (Chapter 4, Statutes of 2009); FCARL 2009-01

FCARL No. 2011-01 - Revised Group Home Audit Protocols


Other Resources

Continuum of Care Reform
http://www.childsworld.ca.gov/PG2976.htm

In September 2012, CDSS in partnership with the County Welfare Directors Association of California (CWDA) launched the Continuum of Care Reform (CCR) effort. Authorized through Senate Bill (SB) 1013 (Statutes of 2012), the CCR will develop recommended revisions to the state’s current rate setting system, auditing procedures and regulations, services and programs serving children and families in the continuum of Aid to Families with Dependent Children – Foster Care (AFDC-FC) eligible placement settings.

California Board of Accountancy
http://www.dca.ca.gov/cba/
California Secretary of State Business Portal

Information needed to start and file a business entity in the State of California, including general information, forms, and fees for corporations. A link is available to the California Corporations Code containing statutory requirements for non-profit corporations in California.

Internal Revenue Service

What you need to know if your organization plans to apply for tax exemption.
Compliance guide for public charities.
2015 Standard Mileage Rates - Notice 2014-79
2015 Standard Mileage Announcement
Helpful Definitions in 2 CFR Part 200

§ 200.12 Capital assets.

*Capital assets* means tangible or intangible assets used in operations having a useful life of more than one year which are capitalized in accordance with GAAP. Capital assets include:

(a) Land, buildings (facilities), equipment, and intellectual property (including software) whether acquired by purchase, construction, manufacture, lease-purchase, exchange, or through capital leases; and

(b) Additions, improvements, modifications, replacements, rearrangements, reinstallations, renovations or alterations to capital assets that materially increase their value or useful life (not ordinary repairs and maintenance).

§ 200.20 Computing devices.

*Computing devices* means machines used to acquire, store, analyze, process, and publish data and other information electronically, including accessories (or “peripherals”) for printing, transmitting and receiving, or storing electronic information. See also §§ 200.94 Supplies and 200.58 Information technology systems.

§ 200.26 Corrective action.

*Corrective action* means action taken by the auditee that:

(a) Corrects identified deficiencies;

(b) Produces recommended improvements; or

(c) Demonstrates that audit findings are either invalid or do not warrant auditee action.

§ 200.33 Equipment.

*Equipment* means tangible personal property (including information technology systems) having a useful life of more than one year and a per-unit acquisition cost which equals or exceeds the lesser of the capitalization level established by the non-Federal entity for financial statement purposes, or $5,000. See also §§ 200.12 Capital assets, 200.20 Computing devices, 200.48 General purpose equipment, 200.58 Information technology systems, 200.89 Special purpose equipment, and 200.94 Supplies.

§ 200.48 General purpose equipment.

*General purpose equipment* means equipment which is not limited to research, medical, scientific or other technical activities. Examples include office equipment and furnishings, modular offices, telephone networks, information technology equipment and systems, air conditioning equipment, reproduction and printing equipment, and motor vehicles. See also Equipment and Special Purpose Equipment.
§ 200.53 Improper payment.

(a) *Improper payment* means any payment that should not have been made or that was made in an incorrect amount (including overpayments and underpayments) under statutory, contractual, administrative, or other legally applicable requirements; and

(b) *Improper payment* includes any payment to an ineligible party, any payment for an ineligible good or service, any duplicate payment, any payment for a good or service not received (except for such payments where authorized by law), any payment that does not account for credit for applicable discounts, and any payment where insufficient or lack of documentation prevents a reviewer from discerning whether a payment was proper.

§ 200.61 Internal controls.

*Internal controls* means a process, implemented by a non-Federal entity, designed to provide reasonable assurance regarding the achievement of objectives in the following categories:

(a) Effectiveness and efficiency of operations;

(b) Reliability of reporting for internal and external use; and

(c) Compliance with applicable laws and regulations.

§ 200.62 Internal control over compliance requirements for Federal awards.

*Internal control over compliance requirements for Federal awards* means a process implemented by a non-Federal entity designed to provide reasonable assurance regarding the achievement of the following objectives for Federal awards:

(a) Transactions are properly recorded and accounted for, in order to:

(1) Permit the preparation of reliable financial statements and Federal reports;

(2) Maintain accountability over assets; and

(3) Demonstrate compliance with Federal statutes, regulations, and the terms and conditions of the Federal award;

(b) Transactions are executed in compliance with:

(1) Federal statutes, regulations, and the terms and conditions of the Federal award that could have a direct and material effect on a Federal program; and

(2) Any other Federal statutes and regulations that are identified in the Compliance Supplement; and

(c) Funds, property, and other assets are safeguarded against loss from unauthorized use or disposition.
§ 200.66 Management decision.

*Management decision* means the evaluation by the Federal awarding agency or pass-through entity of the audit findings and corrective action plan and the issuance of a written decision to the auditee as to what corrective action is necessary.

§ 200.69 Non-Federal entity.

*Non-Federal entity* means a state, local government, Indian tribe, institution of higher education (IHE), or nonprofit organization that carries out a Federal award as a recipient or subrecipient.

§ 200.70 Nonprofit organization.

*Nonprofit organization* means any corporation, trust, association, cooperative, or other organization, not including IHEs, that:

(a) Is operated primarily for scientific, educational, service, charitable, or similar purposes in the public interest;

(b) Is not organized primarily for profit; and

(c) Uses net proceeds to maintain, improve, or expand the operations of the organization.

§ 200.74 Pass-through entity.

*Pass-through entity* means a non-Federal entity that provides a subaward to a subrecipient to carry out part of a Federal program.

§ 200.80 Program income.

*Program income* means gross income earned by the non-Federal entity that is directly generated by a supported activity or earned as a result of the Federal award during the period of performance. (See § 200.77 Period of performance.) Program income includes but is not limited to income from fees for services performed, the use or rental or real or personal property acquired under Federal awards, the sale of commodities or items fabricated under a Federal award, license fees and royalties on patents and copyrights, and principal and interest on loans made with Federal award funds. Interest earned on advances of Federal funds is not program income. Except as otherwise provided in Federal statutes, regulations, or the terms and conditions of the Federal award, program income does not include rebates, credits, discounts, and interest earned on any of them. See also § 200.407 Prior written approval (prior approval). See also 35 U.S.C. 200–212 “Disposition of Rights in Educational Awards” applies to inventions made under Federal awards.
§ 200.84 Questioned cost.

*Questioned cost* means a cost that is questioned by the auditor because of an audit finding:

(a) Which resulted from a violation or possible violation of a statute, regulation, or the terms and conditions of a Federal award, including for funds used to match Federal funds;

(b) Where the costs, at the time of the audit, are not supported by adequate documentation; or

(c) Where the costs incurred appear unreasonable and do not reflect the actions a prudent person would take in the circumstances.

§ 200.85 Real property.

*Real property* means land, including land improvements, structures and appurtenances thereto, but excludes moveable machinery and equipment.

§ 200.92 Subaward.

*Subaward* means an award provided by a pass-through entity to a subrecipient for the subrecipient to carry out part of a Federal award received by the pass-through entity. It does not include payments to a contractor or payments to an individual that is a beneficiary of a Federal program. A subaward may be provided through any form of legal agreement, including an agreement that the pass-through entity considers a contract.

§ 200.93 Subrecipient.

*Subrecipient* means a non-Federal entity that receives a subaward from a pass-through entity to carry out part of a Federal program; but does not include an individual that is a beneficiary of such program. A subrecipient may also be a recipient of other Federal awards directly from a Federal awarding agency.

§ 200.94 Supplies.

*Supplies* means all tangible personal property other than those described in § 200.33 Equipment. A computing device is a supply if the acquisition cost is less than the lesser of the capitalization level established by the non-Federal entity for financial statement purposes or $5,000, regardless of the length of its useful life. See also §§ 200.20 Computing devices and 200.33 Equipment.