

SELECTED AREAS OF COST

Chapter 25 – Entertainment Costs

Authoritative Sources

[FAR 31.205-14](#)
Entertainment costs.

[FAR 31.001](#) Definitions

[FAR 31.201-2\(d\)](#)
Determining Allowability

[FAR 31.2 01- 6](#). Accounting
for unallowable costs.

This chapter provides general audit guidelines for auditing entertainment related costs. Entertainment costs are costs of amusement, diversions, social activities, membership in social clubs or other organizations having a similar purpose, and any directly associated costs such as tickets to shows or sports events, meals, lodging, rentals, transportation, and gratuities.

Background

Federal Acquisition Circular (FAC) 90-31, effective October 1, 1995, implemented requirements from section 2192 of the Federal Acquisition Streamlining Act of 1994, Public Law 103-355. Congress required FAR 31.205–14 to include a statement that costs made specifically unallowable under that cost principle are not allowable under any other cost principle. To avoid confusion, Congress also required the removal of the references to FAR 31.205–1 and FAR 31.205–13. These changes clarified that entertainment costs are not allowable under any other cost principle. Therefore, if the audit team identifies entertainment costs, FAR 31.205-14 takes precedence over any other cost principle. Entertainment costs are expressly unallowable, including any directly associated costs.

General Audit Guidelines

Costs incurred for certain types of activities are clearly entertainment, such as playing golf with current or prospective customers, holiday parties, attending sporting events, or visiting a winery, etc. Other activities require auditor judgment when evaluating the evidence to determine the nature of the activity that generated the cost.

Contractors routinely establish separate accounts to record unallowable costs to comply with the criteria in FAR Part 31. However, allowable activities may have entertainment costs comingled with them. The costs of comingled activities may be recorded in the same or different accounts.

Social activities, including those designed to influence and build relationships, may be an integral part of normal business activities, but that does not make the costs allowable. The costs for other normal business activities such as business meals may be deductible expenses for tax purposes. However, deductibility for tax purposes does not make the cost of an activity allowable (see Chapter 70 for additional detail on business meals). Corporate celebrations are another common business activity that

typically involves unallowable entertainment. The cost of ceremonies like these are also specifically called out as unallowable under FAR 31.205-1(f)(4).

FAR 31.201-2(d) requires contractors to maintain adequate supporting documentation to demonstrate that claimed costs comply with the applicable cost principles. However, this requirement does not mandate a prescriptive list of documentation. Therefore, the audit team should examine all documentation provided by the contractor and evaluate the totality of the evidential matter in making their determinations. Each audit requires auditor judgment based on the unique facts and circumstances.

Audit Considerations:

Comingled allowable and unallowable costs:

The comingling of entertainment with other activities may result in costs being included in various accounts. Auditors should be alert for:

- Recorded costs that are clearly entertainment in accounts other than an unallowable account.
- Labor costs for the time spent attending or participating in entertainment events or activities.
- Entertainment costs comingled with allowable costs, such as costs for business meetings (Chapter 70) or employee morale (Chapter 24) that include social activities.
- Unallowable entertainment costs in unlikely or unrelated accounts. These are accounts that have no obvious connection with entertainment or other similar social activities, such: as maintenance, landscaping, small tools, equipment, etc.

Note: Charging the costs of entertainment in unlikely or unrelated accounts may be an indication of fraud risk.

Common accounts that may contain entertainment costs include but are not limited to the following:

- Employee morale
- Travel
- Recruitment
- Conferences
- Meetings
- Trade, business, or technical professional activities
- Ceremonies
- Training
- Selling
- Awards

Audit Considerations:

- Consulting
- Miscellaneous

Examples:

Incurred Cost Audits:

The contractor sponsors an annual company picnic and claims all associated costs as allowable. The first two hours are spent presenting safety awards (business portion) followed by eating, playing golf and socializing (entertainment portions). Only the costs associated with the awards presentation (e.g., facility reservation fees for the first two hours) are allowable. The cost of food, golf fees, and reservation fees, including the time spent in non-business activities, are unallowable entertainment costs.

Pricing Proposal Audits:

A contractor submitted a proposal that includes a RFP requirement to hold recurring progress meetings with its subcontractors. The contractor believes the requirement implies building rapport with the subcontractor and, therefore, includes costs for rapport-building events, such as a holiday party or a picnic. However, unless the activities are explicitly stated in the RFP, the costs representing entertainment (holiday party or picnic) are unallowable.

Directly Associated Costs

The cost principle provides some examples of directly associated costs. These are not the only directly associated costs the audit team might encounter. The audit team should apply judgment when evaluating costs that are potentially directly associated. The definition of directly associated costs in FAR 31.001 provides a useful framework for determining what costs may be directly associated.

Frequently Asked Questions

Question 1: Does the presence of alcohol at an event, automatically mean the event is a social activity and therefore unallowable?

Answer: The presence of alcohol at an event is only one piece of evidence. The auditor should examine all of the evidence before drawing a conclusion. Alcohol is unallowable under a separate cost principle; FAR 31.205-51. While the presence of alcohol is an indicator that the event may be an unallowable social activity per FAR 31.205-14, it is not itself proof that the event is entertainment since alcohol may be consumed during events that would otherwise be allowable. The auditor should evaluate the totality of the evidential matter in making their determinations.

Question 2: Are the costs of entertainment expressly unallowable for nonprofit and university organizations?

Answer: Yes. [2 CFR 200.438](#) identifies costs for entertainment as expressly unallowable, except for specific costs that have a programmatic purpose and are authorized either in the approved budget for the Federal award or with prior written approval from the Federal awarding agency.