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# **Full Cost Accounting Proposal**

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**BOG Meeting  
November 6, 2005  
Orlando, Fla**

# Full Cost Accounting

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## Background:

- Full Cost Accounting approved by BOG as an FY 06 initiative

## Objective:

- Assign all costs (direct, indirect, and G&A) to programs

# Allocating Costs

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The Federal Acquisition Regulation (FAR 21.201-4) "Determining Allocability" defines 3 allocability tests:

- a) Is incurred specifically for a contract (ASME = project or product)
- b) Benefits both the contract and other work, and can be distributed to them in reasonable proportion to the benefits received or
- c) Is necessary to overall operation of the business although a direct relationship can't be shown

# Allocating Costs

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The DoD (Dept of Defense) states: G&A expenses are incurred for the general management and administration of a business unit as a whole. They must be allocated to a final cost objective on a basis that measures the total activity of the business unit. G&A expenses are intended to have a direct causal or beneficial relationship with any intermediate or final cost objective

## Observations - "G&A"

The Indiana University National Center on Nonprofits and Philanthropy conducted a Nonprofit Overhead Cost Project that included data collected from 1999 to 2004 from about 150 organizations. The following statements are cited from that report.

*"By **organizational infrastructure** we mean accounting, fundraising, information technology, human resources, physical plant and other common organizational elements that undergird a nonprofit's mission and programs. For better or worse, the percentage of total expenses going to program costs is the most common measure of nonprofit organizational efficiency."*

# Definitions for ASME

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**Direct Expense:** Costs are assigned based on an agreed upon usage-based metric. The services related to these assigned costs are structured as shared services to gain ease of operation or economies of scale. The metric column represents the method by which these costs are distributed.

**Indirect Expense:** Costs are related to ASME operations that cannot be distributed based on a usage-based metric. These costs should be allocated based on some agreed upon algorithm. The allocation could be based on gross expense, revenue, headcount, or other methods.

**Services:** Costs of centralized services allocated based on strictly usage.

# Premise

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Every ASME Unit contributes value to the ASME Mission & it's Members.

- Goal is to establish a process to distribute income and expense in a fair, & equitable manner
- Needs to be understandable for all
- Objective is to find long term solutions

## Benefits

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- More accurate view of unit's/programs real net
  - Allows units to make better choices
- Units/programs would know their allocations at budget development time to better plan
- Better idea of full cost of products & services
- Prices & rates would be developed based upon full costs
- Better management of internal costs
- Leads to good decision making

# G&A Functions

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Supports and represents ASME's mission and the prestige it carries to the profession of mechanical engineers worldwide

- Direct
  - Shared services that may not support entire ASME, but support a specific activity, product, program or department
  - Should be a fair & equitable allocation method

# G&A Functions

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- Indirect
  - Enterprise-wide shared services supporting ASME – based on GAAP (generally accepted acct principles)
  - Should be fair & equitable – not directly attributable to a product or program

# Example: Consulting Expense

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- Direct
  - Consultant is hired to develop specific course content or to instruct a particular course
- Indirect
  - A consultant is hired to evaluate the slate of ASME product and service offerings

# G&A - Direct & Indirect

## Direct

- Honors & Awards
- Facilities
- Corp Communications
- Legal
- IT
  - Systems/servers
  - Common Development
  - Data Operations

## Indirect

- Finance & Acctg
- Payroll
- Admin
- Human Resources
- IT
  - Help
  - Network
- Purchasing
- Strategic Mgt
- Executive
- BOG

# Services (usage/activity based)

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Could be either direct or indirect

- Sales & Marketing
- Order Processing
- Member & Customer Service
- Event Management
  - Conference Svcs
- Legal - Some
- Warehouse
- Office Services
- New/Other Services – TBD

# Options to Allocate

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- Allocations/Costing could be based upon:
  - Headcount
  - Revenue
  - Expense
  - Floor space
  - Usage/Cost Drivers
  - Time sheets (labor collection)

# Allocation Methodology

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## Direct

- Honors & Awards - Expense
- Facilities – Floor space
- Corp Communications - Expense
- Legal - Usage
- IT
  - Systems/servers - Usage
  - Common Development - Expense
  - Data Operations - Expense

# Allocation Methodology

## Indirect

- Finance & Acctg - Expense
- Payroll - Headcount
- Admin - Expense
- Human Resources - Headcount
- IT
  - Help - Headcount
  - Network - Headcount
- Purchasing – Expense
- Strategic Mgt - Expense
- Executive – Expense
- BOG - Expense

# Usage Means What?

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Usage will be determined by support staff's time spent on a particular project, program or business unit

- A model will be developed to track and monitor time allocated/labor collection for individuals
  - Could be daily, monthly or quarterly
  - Recommendation is quarterly tracking of time
- Budgets will be developed and shared by support departments with service-receiving depts for agreement
- Budget amounts will be charged or "allocated" on a monthly basis in financial statements
- Adjustments or "true ups" will happen at year end based on actuals

## In Summary

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- Direct and indirect charges will be determined during the budget process and “billed out”
  - “True-up” occurs at year-end
- \*\* True up will be a “reasonability” check based on actual support and service provided for the year. This may result in adjustments to cost of services allocated.

## Next Steps

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- **Oct 11:** Proposal presented to COFI for review, input, & approval
- **Oct/Nov:** Socialize and get “buy in” in principle with ASME operating units
  - Encourage input & comments
- **Nov 6:** BOG approves for FY06
  - This allows units sufficient time to plan for 2007 Bgt

## Next Steps

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- **Nov/Dec:** “Run the numbers” for ASME operating units calculating the planned allocated \$ amounts to incorporate into 06 Bgt
  - For Op units review and response
- **December:** Accounting applies approved model (retroactive to July 1)
- **January and beyond:** Post-implementation - ASME monitors/evaluates/refines model
- **Plan & develop 2007 Budget**

# Recommendation

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- Approve & implement full cost accounting methodology beginning FY06
- Use a 3 year “phase in” approach for cost allocations
  - Ex: A \$300k allocation would work as follows
    - FY06 – allocate \$100k
    - FY07 – allocate \$200k
    - FY08 – allocate \$300k

## Benefits:

- Units have more time to plan by “receiving” costs over time vs the full “hit” in year 1
- ASME in total doesn’t change

# Full Cost Accounting

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- Questions
- Comments
- Discussion

# Motion For BOG

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To approve the Full Cost Accounting proposal as presented utilizing the 3 year “phased in” approach for allocations.