

Costing projects & programmes in the voluntary sector

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What this guide aims to do:

Many charities and not for profits separate their so-called 'core' costs and their project costs and fund raise for each separately. In many cases, however, core costs are not the costs of providing a core service but are really overhead costs. Ideally the overhead costs should be spread fairly over all of the projects, so raising funds for the projects will also ensure that all the overhead costs are covered. This guide explains how those overhead costs can be fairly apportioned.

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1. Introduction

Many charities and not for profit organisations draw a distinction between what they call core costs and project costs. However, by core, they usually do not mean the costs of delivering a core service, but instead mean the overhead costs of the organisation. The result is that, when seeking financial support, they end up not asking for the real cost of delivering a project or programme, but rather ask simply for the direct costs.

To be fair, some funders will not provide the total costs of delivering a project, restricting their contribution to overheads to a small additional percentage of the direct costs. This means that voluntary organisations then have to seek their 'core' costs separately, but no-one really likes to fund this. However, many funders do recognise that voluntary organisations will only survive if they are able to raise the money to cover the true cost of delivery of all of their projects. This is sometimes described as full cost recovery.

HM Treasury endorsed the principle of full cost recovery in its 2002 cross cutting review, "The role of the voluntary sector in service delivery", in which it states "Funders should recognise that it is legitimate for providers to include the relevant element of overheads in their cost estimates for providing a given service under service agreement or contract... All departments will incorporate the review's funding recommendations fully into their procurement policies by ensuring that the price for contracts reflects the full cost of the service, including the legitimate portion of overhead costs by April 2006."¹

The challenge for voluntary organisations then is to be able to calculate the real cost of each project or programme. There are a number of ways that this can be done and many organisations already do this. This note is intended as a simple introduction for organisations which are not yet doing this but which have more than one project or activity and a need and desire to apportion overhead costs across projects.

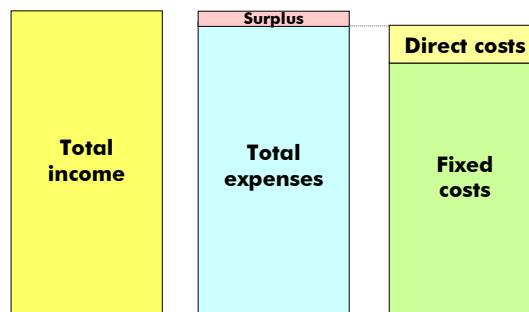
2. Costs

Before you can allocate costs fairly to individual projects, you need to understand what those costs are. A good starting point is to divide costs into different categories.

Some costs can be directly attributed to the production of a product or service and these are usually known as direct costs. Raw materials, bought-in products or services, travel, etc incurred on a specific project are direct costs. Deducting the direct costs from the income for a particular service gives its 'contribution' towards overheads and, once the overheads are all covered, a contribution to surplus. You may also see this referred to as gross profit.

¹ See www.fullcostrecovery.org.uk

Figure 1: Dividing costs

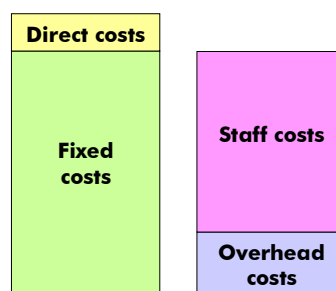


Costs such as rent, rates, insurance, marketing and PR, accounting, audit, staff training, etc do not vary in the short term and are not dependent on the level of production. These are often known as fixed costs, though they can simply be thought of as overheads. It is these costs, with some managerial and other, non-project, salary costs, which voluntary organisations often call 'core' costs, though that is really a mis-description since they are not the costs of providing a core service, but rather the costs of providing the infrastructure which enables the organisation to function.

If you buy capital assets, such as computers, or furniture, or vehicles, you will make an allowance each year, including the year in which the assets are bought, for 'wear and tear'. This is known as depreciation. The money that you spend on capital assets is not an expense, but the depreciation is a legitimate expense and should be included in the overheads.

In figure 1, you will note that there is small surplus shown. Calling voluntary organisations 'not for profit' is slightly misleading. A better description would be 'non profit distributing' since any profit is kept within the organisation and used to further its aims. But some surplus is required to cover the purchase of capital equipment and, as the organisation grows, to provide working capital. It is sensible, too, to build up reserves to give continuity of operation and stability for staff, to provide some funds for initial development work on new ideas before you are in a position to seek funding for them, or to cover unforeseen costs, or if there is a need to make staff redundant.

Figure 2: Dividing costs further



It is possible to take on staff to work on specific projects, and then to let them go at the end of the project, but most organisations prefer to retain people who have built up expertise and experience. This means that, for most organisations, staff costs will also be a fixed cost. However, for the purposes of dividing costs amongst projects, it is helpful to think of staff costs separately from other fixed costs which we will call overhead costs. This gives three costs: direct costs, staff costs and overhead costs.

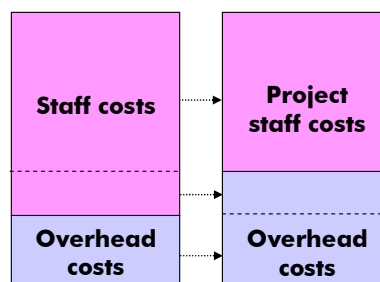
3. Staff costs

Typically, you might expect people working full time to have around 200 days available each year after allowing for holidays, sick leave, etc. It is unlikely that you can charge all of this, for every member of staff, to chargeable projects. Some staff will work all or most of their time on projects; others (such as reception staff, accountants, etc) may not devote any of their time to specific projects, but are necessary for the smooth operation of the organisation. And some, particularly senior managers, may do some project work, but are likely to spend a significant part of their time in managing others or in more general management or in external relations. Let us consider for a moment how to treat staff costs.

Staff who work primarily on projects may be expected to devote most of their time to the projects, though they will still need some time for other things such as staff training, general administration, etc. If you make an allowance of, say, 20 days for this, it leaves 180 days of chargeable time. Use this 180 days to calculate the daily rate used for preparing project budgets and you have automatically covered the cost of the 20 days other time as well. The chargeable time will all be available to deliver (and the cost charged to) every project or programme. When preparing the budget for a project, first consider how many days are required from each person involved and then use this daily rate to calculate the cost.

Senior managers may devote 75 per cent of their time or even more to managerial and non-chargeable tasks; and for reception, secretarial and accounting staff, it is likely that none of their time will be directly charged to projects. The easiest way to deal with this non-chargeable time is to add it back to the overheads.

Figure 3: Allocating staff costs



It is important to minimise the staff time that is part of the overhead, and to maximise the projects, so think carefully about whether there is

anything included in the overheads that could potentially become a project. If you publish a newsletter or annual report, for example, could that be a project – I used to raise sponsorship to cover the cost of producing the annual report.

For most organisations, where staff are contributing to more than one project, and where time is split between overheads and projects, allocating staff time accurately and fairly will require that they keep time sheets. Many organisations do this already; it will add marginally to the paperwork, but is a good discipline and should be very straightforward.

4. Calculating the project cost

The calculation of total project cost is straightforward – it is simply the direct costs associated with that project plus its share of the staff costs plus its share of the overhead costs.

4.1 Direct costs

It should be fairly simple to identify the direct costs for each project or programme. This might include, for example, the costs of renting equipment, or hiring trainers, or undertaking a survey, or travel costs, or printing costs. In the annual accounts, these will probably be shown as a single figure, but in the management accounts they need to be allocated to the correct projects.

4.2 Staff costs

You need to know your staff costs for each project. Calculate a daily rate for each person (or for each grade) by taking the salary costs plus employers' national insurance contributions plus pension contributions plus any other staff benefits and divide by the number of chargeable days. Assess the number of days of each person for each project or programme, and therefore the staff cost, to add to the budget for that project or programme.

Clearly you don't want lots of unutilised staff time, so summarising the allocated days for each member of staff (important if staff are working on more than one project), ideally on a spreadsheet, will help you determine whether anyone is under-utilised or over-worked.

4.3 Apportioning the overhead costs

The total overheads should be calculated – in practice, you will probably do this as part of your budgeting process at the beginning of each year. Ensure that you do include all the costs – including depreciation and the costs of non-chargeable staff time.

The big question, then, is how much of the overheads do you allocate to each project. There are several ways that you could do this. You could simply divide the overheads by the number of projects, so if you have four projects, each carries 25 per cent of the overheads. But if the projects vary in size, this is rather unfair on the smaller projects. You could look at the number of clients who benefit from each project and

divide the overheads accordingly. But the nature of projects might differ, so this may be over-complicated. In most cases, the easiest and simplest way to divide the overheads is in the same proportion as the staff cost allocated to that project. So if a project requires 20 per cent of the chargeable staff time, then it should also carry 20 per cent of the overheads. (If you have staff on secondment, or use large numbers of volunteers, then you may want to ascribe a notional cost, since otherwise projects with unpaid staff will not carry their fair share of the overheads. If you do this, then you will need to use the same figure as part of the income for each project. Indeed, that might be a sensible approach since you may find that you can lever additional support off the back of that in-kind support).

Adding together the direct costs, the project staff costs and the fair proportion of overhead costs gives the total cost for each project.

5. Generating a surplus

If you get this absolutely right, and you are successful in raising the funding required for each project, then you will exactly break even. But, as mentioned above, you need to make a surplus to provide working capital and cover capital expenditure.

You might do this either by including in the overhead an additional amount to cover potential expenditure such as redundancy, or an allowance for premises repairs, etc.

You might do it by allocating more than the 180 days assumed for calculating the daily rate. For example, you might calculate your daily rate on the basis of charging 180 days of a person's time, but actually allocate 190 days to projects (and consequently generate an extra 5 per cent).

You might budget in the expectation of achieving funding for four projects but actually undertake five. You will not make any surplus on the staff cost (unless you are also allocating more than the 180 days of each member of staff) but the overhead costs will all be covered by the first four projects. Add the same proportion to the last project – if you find that the overheads is equal to, say, 30 per cent of the staff cost for the first four projects, then simply add 30 per cent of the staff costs for project number five as well. Provided all the projects go ahead, the last project will generate a surplus.

6. Automate the process

Every organisation is different, so it is difficult to provide a standard template. Doing this on a spreadsheet for all your projects and programmes means that you can ensure that all of your projects, added together, will recover all of your costs. A spreadsheet can also provide a one page summary of your budget on a project by project basis. You can then also use the spreadsheet to prepare monthly management accounts, also on a project by project basis, in order to exercise effective financial control.

7. Example

GF is a charity.

It has a staff of 10 of whom two are wholly administrative (an accountant and receptionist), six are wholly project based and two are managerial (CEO and project director) with their time split between project work and managerial/ administrative work. Annual staff salaries, including national insurance and pension contributions, totals £350,000 which breaks down as shown in the table:

Staff costs

Project staff	210,000
Administrative staff	50,000
Managerial staff	90,000
Total	350,000

GF has annual fixed costs, to cover items like rent, printing, depreciation, utilities, etc of £75,000 per year.

GF has five projects – A, B, C, D and E.

The direct costs (remembering that this does not include staff) for these projects are shown in the table:

Project direct costs

A	20,000
B	30,000
C	40,000
D	10,000
E	25,000
Total	125,000

The total costs for the organisation are, therefore, £550,000.

Summary of total costs

Staff costs	350,000
Fixed costs	75,000
Project direct costs	125,000
Total	550,000

The managerial costs split £40,000 to projects and £50,000 to management and administration which, together with the administrative staff costs of £50,000, is charged to overheads.

The project costs spread across the projects, which depends on the number of days allocated from each person for each project, as shown in the table:

Project staff costs

A	80,000
B	10,000
C	50,000
D	40,000
E	70,000
Total	250,000

We are now in a position to calculate the total cost for each project:

Look at the projects by staff cost and calculate the staff cost for each project as a percentage of the total project staff cost. This is shown in the third column in the table below.

The total overheads comprise the overhead costs of £75,000 together with all the administrative staff and part of the managerial staff, giving a total of £175,000. This should now be allocated across the projects split by the percentage. This is shown in the fourth column.

The direct costs for each project can then be added to give the total cost for each project as shown in the last column.

	Project staff costs	%age	Overheads	Direct costs	Total
A	80,000	32	56,000	20,000	156,000
B	10,000	4	7,000	30,000	47,000
C	50,000	20	35,000	40,000	125,000
D	40,000	16	28,000	10,000	78,000
E	70,000	28	49,000	25,000	144,000
Totals	250,000		175,000	125,000	550,000