

## Full Cost Recovery

### What is Full Cost Recovery ('FCR')

**Full Cost Recovery** means ensuring that all costs involved in running a project are recovered, through securing funding or charging at a level which includes a relevant proportion of organisational costs.

### What do the 'Full Costs' comprise?

The full costs of a project are comprised of '**Direct**' costs – those costs which are incurred as a direct result of delivering a project, i.e.:

- Salaries of people working directly on the project
- Their travel and subsistence
- Materials of other costs directly related to the project



and

**Overhead or 'Indirect' costs** – those needed to manage and support projects and the organisation itself - core costs which are shared amongst the organisation's various activities i.e.:

- Premises hire
- Leadership (Chief Officer)
- Finance (accounting, budgeting, invoicing, purchasing etc.)
- Human Resources (administering, payroll, recruitment etc.)
- IT (purchasing and maintaining computers, email, websites etc.)
- Facilities/Offices (purchasing and maintaining premises, leasing premises, office materials and equipment)
- Other admin tasks (eg answering the phones, managing library resources, data processing etc.).

### Why is FCR so important?

You are not recovering the full costs of your project you are creating a deficit for your organisation. This deficit has to be met through additional fundraising or by using other funds or subsidies to cover any shortfall. This could jeopardise the sustainability of your organisation and hence the services that you provide. By understanding the full costs of a project you can make better informed decisions on which projects you run and how you will fund them. Conversely, it is important for funders to understand the full cost of the service you are providing; the longer- term implications of failing to support these; and for them to obtain transparency regarding costs.

The cost allocation principles of Full Cost Recovery are endorsed by the Charity Commissioners, HM Treasury, a panel representing the voluntary sector that includes funders and are consistent with the Statement of Recommended Practice (SORP).

## Personalisation and FCR:

Southwark Council are commissioning more services through Spot Purchasing. This refers to commissioning individual units of service e.g. lunch club for 1 individual for six weeks. You are paid according to the exact number of units you deliver. Spot Purchasing is already being rolled out in Adult Social Care and will be rolled out for Children and Young People services in September 2014. Full Cost Recovery can help you accurately price 1 unit of your service, so that it can be spot-purchased.

## Principles of full cost recovery:

The principles underlying full cost recovery are:

- Materiality
- Average costs (rather than marginal costs)
- No cross-subsidisation
- Use of cost drivers (any situation or event that causes a change in the consumption of resources)

**Cost centres** are departments that do not generate profit, but cost the organisation money to operate

**Drivers** are the factors that affect whether costs increase or decrease eg

- Headcount to allocate premises
- Time to allocate central function costs
- Expenditure to allocate Governance and Strategic development costs

## Overview of Full Cost Recovery method:

1. Identify your project
2. Identify direct project costs
3. Identify overheads (indirect costs) for your whole organisation
4. Allocate the overheads (indirect costs) to each project
5. Calculate the total cost of each project
6. Calculate the unit cost

## Step 1: Identify Direct Project Costs:

These are costs that are directly incurred as a result of the project. Costs that you might incur if you were starting up a new project are start-up costs: operational/revenue costs: wind down costs. To estimate these, you could look at current projects, or obtain quotes or estimates of hiring items

from Google, or job websites to get an idea of how much you might need to pay somebody for a new post for a new project

## Step 2: Identify your overheads:

Overheads are costs which are necessary for the organisation to operate but do not relate specifically to one project eg lighting, HR costs, premises etc. - **'Cost Centres'** To identify your overhead costs you could refer to your annual accounts or previous management accounts; or Google/obtain estimates. Decide which costs are direct project costs and which are overheads. For example, a small organisation runs a lunch club once a week. It does not run any other work or projects. The lunches, venue hire and any volunteer expenses are direct costs. There are no overheads.

## Step 3: Allocate Overheads

The next step is to allocate overheads between projects. For example, an organisation runs three projects from one building: a lunch club for elderly people, training sessions for single parents and dance classes for members of the community. The organisation would like funding for the training project and has worked out that the project's direct costs include the trainer's salary, books, stationery, a laptop and a projector. The rent and utilities costs are overheads and must be shared fairly between the organisation's three projects. The overheads can be allocated according to **'Cost Drivers'** – the factor that causes a change in the consumption of resources. These might be:

- Floor space occupied
- Headcount (number of staff)
- Staff time
- Time usage of building
- Usage of particular overhead item.

When allocating overheads, the key principles are that the method used should be fair and rational/appropriate.

Different overheads may require different allocation methods – so use the one that seems fairest. It may never be completely accurate but an estimate.

### For example:

The Anytown Children's Project runs a playgroup, and a parents and toddler's group. The direct project costs for the parent and toddler's group is calculated to be £14,000.

The Anytown Children's Centre Manager observes that the time she spends on each project is roughly in proportion to the number of staff working on each project. She and her team also decide staff time is an appropriate basis to share other administration and premises costs amongst the projects. The Centre Manager decides to use the number of staff hours per week as the basis for sharing overheads.

For the next year, the cost of overheads at Anytown will be £64,416.

The staff at Anytown Children's Project will be:

- the centre manager;
- four playgroup staff each working 35 hours;
- The Parents and Toddlers Worker who works 21 hours per week;
- Administrator;
- Cleaner.

\*The centre manager, administrator and cleaner work across all of the projects

How will the share of overheads relevant to each project be apportioned?

<b>Project</b>	<b>Project Staff hours per week</b> (Number of staff x hours worked)	<b>Percentage of Total Hours Per week (Percentage Allocation)</b> (project staff hours per week for that project as % of total staff hours per week)	<b>Share of Overheads</b> (Total overheads x percentage allocation)
Playgroup	4 x 35 = 140	140 divided by 161 x 100= 87%	£64,416 x 87 divided by 100 = <b>£56,041.92</b>
Parents and Toddler	1 x 21= 21	21 divided by 161x100=13%	£64,416 x 13 divided by 100 = <b>£ 8,374.08</b>
Totals	161		<b>£64,416.00</b>

Note: If the project staff worked different numbers of weeks per year (eg some staff worked weeks that other staff didn't), then the number of hours per year would be used to calculate the percentages.

#### Step 4: Calculate Total Cost of Each Project

For each project, add the direct project cost and all the overheads you have allocated to that project.

**Direct Project Costs + Overheads for Project = Total Cost of Project**

#### Step 5: Calculate Unit Costs

The **Unit Cost** is the cost to your organisation of providing each unit of production or delivery. You need to decide what unit of measurement is appropriate for projects in your organisation.

The **Price** is the amount your organisation charges others for a product or service.

**Price** and **Unit Cost** are usually different.

Consider how much your market will bear. Experimenting with different amounts of units of delivery will enable you to understand how much you will need to charge to recover your costs at each level.

### Tip box: Calculating Percentages

One per cent means 1 divided by 100 ( $1 \div 100$ ) that is, one hundredth

- 1% is  $1/100$  expressed as a fraction or 0.01 as a decimal.
- 3% is  $3/100$  or 0.03 as a decimal

To calculate the percentage of a number you multiply the number by the percentage expressed as a decimal:

- 1% of £1000 is  $0.01 \times 1000 = \text{£}10$
- 20% of £1000 is  $0.20 \times 1000 = \text{£}200$
- 45% of £500 is  $0.45 \times 500 = \text{£}225$

## Typical Project Costs

Start-Up	On-going	Close Down
Advertising for, recruiting and training staff and volunteers	Salaries of project workers, including employers' national insurance contribution and any employers pension contributions	Staff redundancy or re-deployment costs
Buying equipment furniture and vehicles	Expenses of project staff and volunteers, including travel, accommodation and phone bills	Disposal of any premises or equipment used specifically for the project including any dilapidation costs
Finding premises and preparing them for use	Rent, heating, lighting, maintenance and insurance for office space and buildings only used for the project	Final project evaluation and reporting.
Promoting the project	Training for staff and volunteers working on the project	
Legal costs involved in negotiating and drawing up contracts	Materials and the day to day running costs of the project	
Obtaining licenses and permits	Items with a short life such as stationary or lightbulbs	
	Monitoring and evaluation of the project	
	Raising funds for continuing the project once the current project is over	

	Marketing and publicity Professional and legal fees incurred specifically for the project	
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## Support

If you would like further support on any of the issues raised here or any other matters, please contact the Development Team at Community Southwark at [development@communitysouthwark.org.uk](mailto:development@communitysouthwark.org.uk)

## Resources

- [Big Lottery Fund](#)
- [Cash Online](#)
- [Community Accounting](#)
- [Funding Central](#)