



Calculating full cost recovery

What is full cost recovery?

Full cost recovery is the process of ensuring that you've taken account of all of the costs involved in running a project by calculating the funding you need at a level which includes both direct project costs and a relevant proportion of overhead costs.

Direct project costs are all the additional costs you'll incur as a result of carrying out a specific project.

Overhead costs are shared organisational costs that support all aspects of an organisation, such as office rent, IT, financial management, human resources etc.

When applying for project funding, it's important you understand the costs and whether you wish to apply for full cost recovery. Otherwise you may be creating a deficit for your organisation, which will need to be generated from other sources. This in turn can impact on the sustainability of your organisation as well as the quality and longevity of the services you provide.

The method

In simple terms, there tend to be three categories of costs:

Staff costs:

It is possible to recruit staff for a limited term to work on a particular project and for them to leave at end of the project, but most organisations prefer to retain people who have built up expertise and experience so, in most cases, staff costs will also be fixed costs. But for the purposes of dividing costs amongst projects, it is helpful to think of staff costs separately from other fixed or "overhead" costs. You'll also need to think through what is reasonable in terms of available chargeable time. 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 be involved in oversight, quality assurance or supervision of the project, but are likely to spend a significant part of their time in managing others or in more general management or in external relations or business development. 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 the 180 days (rather than the 200) to calculate the daily rate used for preparing project budgets and you will automatically cover the cost of the 20 days other time as well.

Other direct costs:

These are the costs that arise as a direct result of running the project – raw materials, bought-in products or services, travel, etc

Fixed (“overhead”) costs:

Costs such as rent, rates, insurance, marketing and PR, accounting, audit, staff training, etc and are not dependent on the level of activity in the short term (although long term, if your activity increases significantly and you need bigger premises, for example, then your fixed costs will change, but let’s not complicate things). It is these costs, with some managerial and other, non-project, salary costs, which voluntary organisations tend to refer to as ‘core’ costs, though that is really a misdescription 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. Depreciation on any of your fixed assets such as computers, vehicles etc should also be included here.

Once you’ve got a clear idea of your costs – and the categories they fall into – and have decided on the basis you will allocate your fixed costs to a project – then the process of calculating full cost recovery on your project is much more straightforward.

Allocating fixed (“overhead”) costs to projects

Costs can be divided amongst projects using cost “drivers”. Commonly used cost drivers include:

- **Staff time (remember to include volunteers)**
- **Staff cost**
- **Number of beneficiaries**
- **Floor space**
- **Numbers of staff etc.**

When allocating overheads, the key principles are that the method used should be logical but not over-complicated and that this feels right both to you and your team and to your advisors and funders. You could simply divide the overheads by the number of projects, so if you have four projects, each carries 25% of the overheads. But if the projects vary in size, this is unfair on the smaller projects. You could look at the number of beneficiaries for each project and divide the overheads proportionately. 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 25% of the chargeable staff time, then it should also carry 25% of the overheads. (If you have staff on

secondment, or use large numbers of volunteers, then you may want to apply a notional cost to their time, since otherwise projects with unpaid staff will not carry their fair share of the overheads. If you do this, then you will need include the same figure in the total income for each project).

An example:

XY Charity has a staff of eight and runs a befriending service for socially isolated older people. It has decided that it wants to run a year-long pilot project to test a new approach to running a lunch club.

One member of staff is wholly administrative and two are managerial (CEO and finance manager) with their time split between project work and the ongoing management and administration of the charity. Annual staff salaries, including national insurance and pension contributions are as follows:

Staff costs

Direct service staff (5 FTE) £50,000

Administrative staff (1 FTE) £25,000

Managerial staff (2 FTE) £70,000

Total £145,000

Fixed (“overhead”) costs

XY has annual fixed costs, to cover items like premises, printing, depreciation, heat, light, etc of £50,000 per year.

Direct costs

Direct costs for the lunch club pilot (not including staff costs) £11,000

Other direct costs of running ongoing service: £100,000

Summary of total costs

Staff costs £145,000

Fixed costs £50,000

Direct costs £111,000

Total £306,000

Allocation method

The fixed cost allocation method will be on the basis of staff cost.

The administrative and managerial staff costs are estimated to split £10,000 to the project and £85,000 to the ongoing running of the services. It's been estimated that the equivalent of one full time equivalent member of the service staff team for the full year will be allocated to the pilot project.

	Staff costs (£)	%	Overhead allocation (£)	Direct costs (£)	Total (£)
Lunch club pilot (12 month project)	20,000	14	7,000	11,000	38,000
Ongoing service	125,000		43,000	100,000	268,000
TOTAL	145,000		50,000	111,000	306,000

*** £10k direct staff cost (one out of the five) plus £10k admin and managerial staff cost**

So the total cost of running the lunch club pilot for a year is estimated to be £38,000.

Generating a surplus

If you are successful in raising the funding required for each project, (and, of course, you've estimated your costs correctly) then you will break even.

But you need to make a surplus to provide working capital and cover capital expenditure or to build up your reserves. 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.

Alternatively, you might budget in the expectation of achieving funding for two projects but actually undertake three. You will not make any surplus on the staff cost (unless you are also allocating more than your assumed number of days of each member of staff) but the overhead costs will all be covered by the first two projects. If you apply your average assumed overhead rate to the third project and provided all the projects go ahead and are funded, the last project will generate a surplus.

Also check out the following page and resources:

NCVO's Project budgeting and full cost recovery

<https://knowhow.ncvo.org.uk/organisation/financial-management/planning-and-budgeting/project-budgeting-and-full-cost-recovery>