

Social Justice

Full Cost Recovery in the Voluntary Sector – Impact Assessment

Keith Hayton, Vincent Percy and Karen Crawford
GEN Consulting

Full Cost Recovery (FCR) is the principle that, when entering into a contract with a public body, the service deliverer should be able to recover all of the costs associated with that contract. The Scottish Executive, in the Scottish Compact, made a commitment to recognise the need for FCR in bids made by the voluntary sector. Despite this commitment, the cost of implementation was not known. This study was commissioned to estimate these costs and look at some of the wider implications of FCR implementation.

Main Findings

The main findings of the study were that:-

- The voluntary sector in Scotland delivers a wide variety of services for public bodies. Contracts for these range in value from small ones, of less than £50,000 a year, to those in excess of £1 million;
- The majority of these contracts are delivered at less than full cost, that is the value of the contract is judged not to cover the direct costs of service delivery and the related overhead costs (such as management and administration) that any organisation has to cover if it is to survive;
- Of the contracts identified, 71% were not explicitly based upon FCR. The estimated extent of underfunding of the survey respondents was £2.55 million, or 0.96% of their total income;
- Voluntary organisations tended to cover the gap between their full costs and the value of contracts by running down reserves. The implementation of FCR was seen as a way of building up reserves and improving the quality of service delivery;
- Voluntary organisations that attended Focus Groups had, in the absence of many funders paying their full costs, developed a number of survival strategies including cross subsidy and presentation of costs in different ways to different funders;
- The Focus Group attendees were sceptical about FCR being introduced. However, if it were, they felt that it would mainly benefit the larger voluntary organisations;
- The public sector interviewees felt that the introduction of FCR would, over the longer term, be detrimental to the sector as voluntary providers would be displaced by private sector competitors and public bodies would cease to buy some services from the sector due to lack of funds; and
- When the estimated extent of contract underfunding from the sample of voluntary organisations was corrected, and grossed up to the population of voluntary bodies within Scotland, the annual cost of implementing FCR was estimated to be £118 million or 4.5% of the sector's estimated annual income.

Background

FCR is the principle that, when delivering a service for a public body, a voluntary organisation should be able to cover the direct costs of service provision, all of the indirect costs associated with that service and a proportion of the organisation's overhead costs. The Strategic Funding Review identified FCR as a key factor in ensuring that the voluntary sector is sustainable. Whilst all of the partners in the Review (the Scottish Executive, the Convention of Scottish Local Authorities and the Scottish Council for Voluntary Organisations) have accepted, in principle, that funding relationships between public and voluntary bodies should be based on FCR, the costs and potential impact are uncertain. To explore these issues in more detail this study was commissioned.

The Voluntary Sector Survey

A survey of 100 voluntary organisations was undertaken. This was designed to be representative of the sector and excluded (as far as possible) those organisations with incomes of less than £25,000, as it was felt that FCR was unlikely to be relevant to them.

The organisations were asked to give details of the four largest contracts they had with the public sector. Of the ones identified 71% were not explicitly based on FCR. The extent of estimated underfunding of the respondents by public funders for whom they were providing services was £2.55 million. The larger organisations, those with annual incomes over £1 million, accounted for 56% of this sum.

Voluntary Sector Focus Groups

What emerged strongly from the three Focus Groups was that most organisations had evolved funding survival strategies in the absence of FCR's implementation. As funders often did not want to fund management or administrative costs, these strategies involved such things as describing posts in different ways to different funders so that it was possible to draw together a variety of funding streams to cover overhead costs.

When the reasons for organisations continuing to provide services for public bodies at less than full cost were explored, the explanation that emerged was the "voluntary sector ethos". This can be defined as a desire to meet local needs that others either do not recognise or are unwilling or unable to meet. One consequence of this was that voluntary bodies were either taken for granted or were exploited.

Best Value was, in the experience of all of those who were familiar with it, interpreted as being about lowest cost. Given this, the ability of voluntary bodies to differentiate themselves from commercial providers through Best Value was thought to be limited.

The Public Sector Interviews

Nineteen people from public sector organisations were interviewed. There was a general view that there was a need for education and training across the public and voluntary sectors. This would enable public bodies to apply Best Value and to adopt fair and transparent commissioning arrangements. The voluntary sector would be helped to "sell" itself more effectively to funders.

The local authority interviewees were largely opposed to FCR being introduced without additional finance being provided to cover the costs involved.

Trust

What permeated the Focus Groups and the public sector interviews was a lack of mutual trust. The voluntary sector felt it was exploited by public funders, whilst the public funders thought that the sector saw FCR as giving it a blank cheque. Addressing this issue of trust seems to be crucial if FCR is to be implemented.

The Cost of Implementing FCR

To correct bias in the survey sample there was a need to correct the sample distribution across annual income bands and to factor this distribution up to the total size of the sector in Scotland. This process was difficult as there is no single comprehensive and accurate data source about the "shape" of the sector in Scotland.

It was decided that those voluntary organisations with incomes of less than £25,000 a year would be removed from the calculations. The assumption was that FCR was likely to be of limited relevance to these small organisations, most of which are volunteer run and are reliant upon a single funding source.

This resulted in there being an estimated 15,500 voluntary organisations within Scotland having incomes in excess of £25,000. Based on the extent of estimated underfunding of the organisations surveyed, it was calculated that the annual direct cost of implementing FCR was between £106 million and £130 million, with a mid-range estimate of £118 million.

This ranges from 4.1% to 5.0% of the sector's estimated annual income.

Action Points

The study concluded with 16 Action Points. The main ones were:-

- The promotion and development of the National and Local compacts would be a way of beginning to develop greater trust between the voluntary and public sectors;
- This would be helped if public funders involved the sector in discussions when formulating policy and funded voluntary organisations for longer than one year;
- Best Value needs to be promoted to local authorities in a way that stresses that it is about more than cost;
- Voluntary organisations should be willing to withdraw from providing services if they are not paid full costs;
- The Strategic Funding Review partners need to reach agreement on those items that are eligible for inclusion in any FCR model and the type of funding relationships to which it will apply;

- The Executive should consider the increased costs faced by the public sector in implementing FCR and how these should be reflected in their financial allocations;
- Consideration should be given as to whether "one-off" support should be given to cover training costs; and
- Training should be provided for the voluntary sector and public bodies to make them aware of the theory and practical implementation of FCR.

Research Methods

The Impact Assessment involved a number of elements. These included: a literature review; a survey of 100 voluntary organisations operating in Scotland; three Focus Groups with voluntary organisations in rural, semi-rural and urban areas; interviews with public sector employees in the Scottish Executive, local authorities and Non-Departmental Public Bodies; and a number of FCR practice case studies of voluntary organisations and public bodies.

If you have any enquiries about social research, please contact us at:

Scottish Executive Social Research
1-F (Dockside)
Victoria Quay
EDINBURGH
EH6 6QQ

Tel: 0131 244-7565

Fax: 0131 244-7573

Email: socialresearch@scotland.gsi.gov.uk

Website: www.scotland.gov.uk/socialresearch

The report, "Full Cost Recovery in the Voluntary Sector – Impact Assessment", which is summarised in these Research Findings, is a web-only document and is available on the Social Research website at:

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