



Appendix B: Programme Efficiency Benchmarking Exercise

The organisational implications report provided an overview of a suggested organisational strategy, proposing practical organisational systems, and structures, in order to implement the institutional strategies identified in the South African Cities Network's (SACN) Strategic Outlook. The overall strategic evaluation of the SACN aims to develop a direction for the organisation, to inform and guide business planning processes. The suggested Organisational Strategy seeks to inform SACN business planning for organisation's next strategic cycle (2016-2021). The position put forward by the strategic report is that the SACN is currently at a strategic crossroads and in need of a revised strategy to strengthen its mandate going forward. The organisational strategy recommends system and structural responses to implement the institutional strategy, thus informing the business planning cycle. These recommendations take the form of a sourcing strategy and an organisational structure.

From a practical, implementation perspective, both the sourcing strategy and the organisational structure have an impact on the size of the organisation. However, before finalizing the recommendation on the organisational size, it is important to explore the other factors influencing the organisational size. One factor that constrains the growth of the organisation is the internal policy to maintain expenditure on core programme costs at 30 percent of total expenditure. This is to ensure that at least 70% of expenditure is allocated to programme costs.

This benchmarking exercise explores the rationale for the 70/30 expenditure decision and investigates its impact on programme efficiency. To achieve this, international requirements around programme efficiency ratios are reviewed, together with the way in which local NGOs reflect programme efficiency ratios. The benchmark also explores the way in which local NGOs manage staff costs (in comparison to the SACN). Finally, this benchmarking exercise utilises the findings to present recommendations to the SACN regarding organisational health indicators.

B.1. Status Quo Assessment

a. SACN Organisational Status Quo

In order to make recommendations on programme efficiency indicators, it is important to understand what the current organisational position on salary costs is and the rationale for this position. As mentioned above, the current position is that salary costs should be less than 30% of total expenditure, leaving 70% of budget allocated to programme costs.

The logic for this 30/70 programme efficiency ratio is clear. The starting point is a desire to measure programme efficiency and demonstrate value to funders. The need for accountability in NGO funding is an international trend and ensures that donor money is allocated wisely and fairly. One of the ways in which the SACN seeks to uphold accountability is by ensuring the ratio of core costs to programme costs (programme efficiency ratio) is low, with the majority of the budget being allocated to programme costs. The SACN currently classifies staff costs as part of core costs. This means that salary costs, even if they are related to programme activities, are restricted by the current core cost to programme cost ratio if the aim is to keep core costs to a minimum, there is limited scope to increase salary expenditure.

The rest of this document explores the way in which programme and core costs (also known as direct and indirect costs) are described and funded using international and domestic approaches, and how the SACN staff costs compare



to similar local NGO staff costs. The benchmarking exercise seeks to establish the following: the common treatment of programme efficiency indicators, the common treatment of direct and indirect costs, and exploring what a reasonable benchmark for staffing costs could be.

b. International Donors

In order to obtain a holistic understanding of indirect cost or core funding, it is necessary to gain an international perspective on this issue. This section defines the programme efficiency requirements of international donors. The first step is to provide a definition of indirect costs, followed by a comparison of donor policies regarding indirect costs. The general trend is that most international donors refer to direct and indirect costs, rather than programme and core costs.

The Bill and Melissa Gates Foundation offers the following definition of indirect costs:

- *Overhead expenses or ongoing operational costs incurred by the applicant organization on behalf of the organization’s activities and projects, but that are not easily identified with any specific project.*
- *Administrative or other expenses which are not directly allocable to a particular activity or project.*
- *Expenses related to general operations of an organization that are shared among projects and/or functions.*
- *Basic examples include executive oversight, existing facilities costs, accounting, grants management, legal expenses, utilities, and technology support.*

This definition does not clearly equate indirect costs with staffing costs. This understanding is shared by the Department for International Development (DFID) which recognises that some core costs are required in order for projects to function – for example the cost of facilities. DFID states that they are willing to fund such costs, and that the recovery of indirect costs related to programme activities should be profit neutral. In other words, organisations should not make a profit from DFID funding, while at the same time DFID should not benefit from under-funding core costs.

Below is a table of selected donor foundations, their definition of indirect cost (where available) and their policies around indirect costs, and the percentage allocated to indirect costs.

Table 1: International donor indirect funding policies

Donor	Indirect Cost definition	Percentage Allocated
DFID	Direct eligible costs are those which support all aspects of the research, training and dissemination activities of the project (including salaries of relevant officials)	20%
Carnegie	No fixed policy	10-15%
Ford Foundation	Decisions made on a case-by case basis	Up to 10%
Bill and Melissa Gates Foundation	Only justified indirect costs	Up to 10%
Open Society	Depends on nature of the project	Up to 10%
Skoll		Up to 18%



Analysis of the table above shows that most of the funders described above have an indirect cost ceiling of 10% of project costs. It is important to note, however, that all the foundations discuss this in terms of general rules, including the following:

- Organisations should substantiate claims for indirect costs and funders may fund less or more than 10% accordingly.
- Funders place a greater emphasis on the importance of programme outcomes.
- None of the organisations prohibit staff costs being included in direct costs.

c. South African NGOs

Having established an idea of international practice in terms of indirect costs and staff salaries, it is important to establish a reference point for South African practice. This section provides a view on the way in which South African NGOs classify direct and indirect costs as well as the proportion of budgets commonly allocated to staff expenses.

Various regulations around NGO transparency require NGOs to make their financial statements available. The funding applications which discuss core and programme costs are confidential. An interview with a local fundraiser, who has raised money internationally and locally, confirmed that it is local practice to allocate staff costs, including some senior management supervision time, to direct programme costs.

The Institute of Justice and Reconciliation (IJR) is an interesting case study because they make their direct and indirect cost publication public as well as their staff allocations.

Table 2: IJR staff costs and programme costs

Costs	
Management and admin costs	R4.7 Million
Programme costs	R26.58 Million
Salary costs	R11,299 Million
Total expenses	R31,29 Million

Mothers2mothers (M2m) is another South African NGO that discloses direct and indirect costs, with programme costs being estimated at 92% and core costs at 8%. Because the NGO employs at least 1250 people, it is safe to assume that some of the staff costs are allocated to programme costs. M2m has an emphasis on measuring programme outputs, which helps to reassure funders that their money is being spent wisely.

Although many NGOs do not divulge the programme versus core cost calculations, many do disclose their audited financial statements. These statements give an indication of staff costs in proportion to expenditure on the budget. The NGOs chosen for the survey are well-known NGOs working in the knowledge production and advocacy space. The staff expenditure to expense ratio was chosen because a number of organisations carried a surplus year on year. It is clear from this that some staff costs are allocated to programme costs. In addition the ratio of indirect costs to direct costs seems consistent with international practice. The ratio staff costs to other costs seems consistent with the South African NGO standards laid out in the table below.



Table 3: South African NGO staff costs

NGO	Date	Size	Staff Costs	Expenditure	Percentage of expenditure spent on staff costs
South African Institute of Race Relations	2014	25	R 9.2 Million	R 12.69 Million	72%
Section 27	2012/2013	31	R10.55 Million	R 18.62 Million	56.66%
Inyathelo	2015	19	R7.54 Million	R20.41 Million	36.9%
Ndifuna Ukwazi	2013	15	R2.3 Million	R3,2 Million	71.8%
Action Aid international	2014	31	R9.2 Million	R22.87 Million	40.2%
SACN	2014		R12.92 Million	R47 Million	27.4

As can be seen, in the table above, the SACN staff to expenditure ratio is the lowest of all the organisations surveyed. Both the South African Institute of Race Relations and Section 27 both perform research functions in-house, whilst the SACN outsources much of its research production. Even though the SACN outsources research production, research managers do sometimes step into a research production role.

B.2. Findings

In order to demonstrate value for money and effectiveness, the SACN keeps track of its programme efficiency ratio (i.e. programme versus core cost). The current practice is that indirect (or core) costs should be kept at under 30% of the budget. The current definition is that indirect costs are equivalent to staff costs. The benchmarking exercise explored international definitions of direct and indirect costs, and observed cost-ceilings for them. South African practice around direct and indirect costs, as well as staff cost ratios were explored. The following insights emerged from this benchmarking exercise:

- SACN has the lowest staff to expenditure ratio in a group of South African NGOs surveyed but a higher than average indirect cost to direct cost ratio;
- Measuring programme efficiency is an internationally accepted best practice;
- It is recommend that the SACN move towards aligning programme efficiency ratios with international and local practice;
- In order to achieve this, it is recommended that programme staff costs be calculated as part of direct programme costs, as well as programme management time spent by senior managers;
- We note that the SACN's staff portion of the annual budget is low relative to all other NGO's surveyed. Based on this status quo, some expansion based on programme needs should not be avoided.