

# Understanding administration costs and capacity building

Understandably, many givers are concerned about funding unnecessary or excessive administration costs, especially marketing and communications, fundraising appeals, direct mail, merchandise catalogues and high-cost events. While it's always your prerogative to stipulate your 'no go' areas – and charities are generally very accommodating of a donor's wishes – it's worth interrogating assumptions about 'administration', before ruling out such funding altogether.

## The finer points of definition

Australia has no clear definitions or mandatory accounting practices defining which of a charity's costs should be categorised as 'service-related' and which should be understood as 'overhead', so charities often account for these differently in their financial statements. Meaningful comparison is rendered almost impossible by the sheer diversity of organisations operating in the not-for-profit sector: from large, complex, national structures with extensive programs, through to local, volunteer-led initiatives with no paid staff. What is considered a 'reasonable' administration spend will vary widely.



## Isn't supporting direct service delivery more meaningful?

There is a long-standing perception that funding the indirect costs of an organisation – usually associated with systems, staffing and infrastructure – is somehow less impactful than funding the direct costs of frontline delivery. Often donors are naturally drawn to funding tangible services – the outputs and outcomes of a charity's purpose. But long-term impact is often associated with the degree to which a charity can sustain and scale its operations or adapt to changing external realities - from policy-level pivots to a pandemic. This is the realm of capacity, a far less 'concrete' but incredibly important predictor of an organisation's long-term viability.



## Why fund capacity-building?

In the business start-up world, we routinely deploy the adage 'You have to spend money to make money'. In the for-purpose sector, it is important to recognise that resources are required to run a charity too. Capacity-building funding enables organisations to make strategic investments in the removal of barriers to operation and growth – building internal capability through improved systems and business processes, IT, training, human resources, governance controls or evaluation culture. If you are already partnering with an organisation you love - with a strong and proven mission, expertise in program delivery, and data that evidences its potential and actual impact - it makes sense to help it sustain itself into the future.



We all want a well-run organisation to evolve from good to great.

## Pay what it takes

[Pay What It Takes](#) is movement driven by some of Australia's leading philanthropic foundations that urges funders to fully understand the true costs of charitable work and provide funding that covers all necessary expenses, including administrative and infrastructure costs, rather than restricting funding to specific programs or activities. The work is a collaboration between Social Ventures Australia (SVA), the [Centre for Social Impact](#) and [Philanthropy Australia](#). The full research report is available through the link above, however key take-outs for funders include:



- True indirect costs are not being covered by funders

On average, the true indirect costs of each organisation were 33% of their overall costs. Yet many organisations believe, potentially incorrectly, that funders are mostly unwilling to fund above 20% or, even lower.

- Indirect costs are not a good way to assess charities

Not-for-profits that spend less on indirect costs are not more effective than those who do not. Evidence shows that spending insufficient resources on indirect costs can potentially reduce overall not-for-profit effectiveness.

- Low indirect costs reduce capability and effectiveness

The not-for-profits that participated in the study universally underinvested into their core capability. This increases risk and forces organisations to search for untied funding and introduces inefficiencies.

## Keep communicating

Some donors are concerned about the loss of control associated with providing an 'untied' or unrestricted gift, and whether they'll be able to determine exactly how it's spent and to what effect.



The solution to understanding the impact of any gift is to keep communicating with your charitable partners. It's good practice to develop a mutually agreed understanding of how funding will be spent, and how progress will be charted over time – preferably before any funding is given. Stay in touch with your charitable partners at regular agreed intervals, forging a two-way feedback loop over the course of the funding period. This is more likely to lead to a genuine partnership for social change, based on honesty and trust, rather than a limited-life 'carrot and stick' reporting relationship.