Indirect/Overhead/Shared Costs Policy

Purpose

The purpose of this policy is to establish a fair, consistent, transparent, and auditable method for allocating the organisation's shared overhead and indirect costs to individual projects and programs in accordance with donor agreements, accounting standards, and sound financial management practices.

Definition of Indirect Costs

Indirect costs are those expenses that are not directly attributable to a specific program, project, or activity, but are necessary for the overall operations and management of the organisation. These are also referred to as **overhead costs or shared costs**. These costs support the infrastructure required to deliver programs effectively.

Examples of indirect costs include:

- Administrative salaries (finance, HR, management)
- Office rent and utilities
- General office supplies
- Legal, audit, and accounting services
- Information technology and systems support
- Insurance and compliance-related costs
- General fundraising expenses

Background

As a nonprofit organisation, we incur both direct and indirect costs in carrying out our programs and activities. While direct costs are attributable to specific projects, indirect costs are the shared expenses necessary for the overall functioning of the organisation, without which program activities cannot be delivered effectively

Scope

This policy applies to all programs, projects, grants, and activities of the organisation, including both restricted and unrestricted funding.

Budgeting of Indirect Costs

The organisation uses a **comprehensive budgeting process** to ensure that indirect costs are planned and funded adequately:

1. **Indirect Cost Rate Calculation**: The organization calculates a **provisional indirect cost rate**, typically as a percentage of total direct costs or program expenditures.
2. **Inclusion in Project Budgets**: This rate is applied while preparing budgets for grants, donor proposals, or institutional funding applications.

3. **Compliance with Donor Policies**: The organization aligns with donor-specific caps or guidelines regarding allowable indirect cost recovery, if applicable.

Ensuring Adequate Funding of Indirect Activities

To ensure that essential indirect functions are sustainably funded:

- The organisation maintains a **cost recovery strategy**, which includes negotiating an appropriate **indirect cost rate** with funders.
- Efforts are made to **diversify funding sources**, ensuring not all revenue streams are restricted to direct program costs.
- Where donors do not allow indirect cost recovery, the organisation seeks to fund the shortfall through **unrestricted donations, general funds, or core grants**.
- Regular **cost-efficiency assessments** are conducted to keep indirect costs reasonable and justified.

Allocation Methodology

Basis of Allocation: Shared overhead costs are allocated to individual projects on a percentage basis strictly in accordance with the approved grant budgets subject to the maximum overhead percentage allowed by the respective donor. Therefore, different projects may bear different overhead percentages depending on the donor-approved ceiling.

Limitation

The organisation ensures that total indirect costs charged to projects do not exceed the actual common operational costs incurred by the organisation. Further, any excess overhead costs beyond donor limits are borne by the organisation and not charged to the concerned project

Consistency of Application

The approved allocation percentages are applied consistently throughout the financial Period.

Monitoring and Reporting on Indirect Costs

To ensure transparency and accountability:

- Indirect costs are tracked monthly through the accounting system.
- Reports distinguish between direct and indirect expenditures, ensuring clarity for internal and external stakeholders.
- Annual audits verify the reasonableness and allocation of indirect costs.

Compliance

This policy aligns with generally accepted accounting principles for nonprofit organisations and the specific financial and contractual obligations of donors and regulators.

Conclusion

Through clear policies, systematic budgeting, and regular monitoring, the organisation ensures that **indirect costs are managed efficiently and funded adequately**. This not only supports operational continuity but also promotes financial sustainability and compliance with donor expectations.
