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Indirect costs: Think tank strengthening and sustainability

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**Why is this
important?**



Strengthening and sustainability

- Adequately calculating and funding of indirect costs/overheads is crucial for the **operational sustainability and strategic planning** of think tanks.
- Failure to fully fund these costs can force think tanks' to focus away from their mission to address their **financial strength/survival** instead
- Failure to engage on these issues fuel common misconceptions that affect further reform:
 - **"Low overheads are indicative of efficiency"**
 - "Organisations delivering the same services or functions should have similar business models, scale and operational contexts"
 - "Indirect costs/overheads remain the same over the lifetime of a project"
 - "CEOs and business development are direct costs"



What is the
“indirect cost”?



Definitions matter!

Essential operational costs that are not attributable (or difficult to attribute) to a specific project. These costs are **shared among projects** and among functions within the organisation. Costs are typically classified as indirect when either of two conditions is met (or both):

1. The costs benefit the entire organisation and all projects carried out by the organisation;
2. The costs are attributable to specific projects, but the administrative cost of tracking and allocating these costs to individual projects outweighs the benefit of doing so.

- [Funders for Real Change](#) have defined the term as “administration costs that are necessary to administer and manage the organisation and are shared across all the activities”.
- Eligible costs are not standardised across all funding organisations.

Multiple definitions depending on the funder

| Funder | Definition |
|---------|--|
| Ford | expenditures that are shared across multiple projects or cost centers within an organisation and therefore are difficult or impossible to attribute to a specific project, e.g. accounting, TI, chief executive's office |
| Gates | <p>general overhead and administration expenses that support the entire operations of a grantee and that may be shared across projects. Examples include facilities expenses, e.g. rent, utilities, equipment for the grantee's headquarters, and associated information systems and support and administrative staff such as HR, general finance, accounting, IT, and legal. [...]. While these costs may not be directly attributable to a project, they are real and necessary to operate as an organisation.</p> <ul style="list-style-type: none"> Indirect Cost Rate = Budgeted Indirect costs/ Budgeted Total Direct Costs (e.g. personnel, sub-awards, supplies, equipment, etc.) |
| Hewlett | expenses necessary to support an organisation's general operation, which are thus shared across projects or programs. E.g. rent and utilities, office furniture, computers, IT, development, finance and accounting, HR, and legal. Expenses like these would be incurred in some amount with or without a specific project or programme grant. But, while not incurred solely because of a project or program, they are necessary for the organization to execute it. |
| IDRC | <p>administrative costs that are not directly related to the research. Indirect cost items are limited to:</p> <ul style="list-style-type: none"> salaries and benefits of personnel who support and administer the project, such as secretaries, clerks, and accountants; stationery and other office supplies; telecommunications (unless the nature of the project has warranted a specific budget line item for that purpose); and computer equipment used for the administration or accounting of the grant disbursements. |
| Laudes | costs that cannot be identified within a programme activity but are needed for the general administration of the organisation |

Use different terms that can also mean different things:

- Expenditures
- Overhead

Note: IDRC makes the point of focusing on research and considers the costs directly involved in a project as indirect if they are not directly involved in research.



Initial findings: funders and think tanks



Funders approach to indirect cost and rates...

- There is not a single standard way for defining and calculating indirect cost and rates.
- Definitions and eligible costs vary among funders and think tanks
- The indirect cost rate is commonly calculated as indirect cost/direct cost.
- Funders usually set **caps or ranges for indirect cost rates that vary depending on the type of contract and organisation**. These caps are not necessarily aligned with real indirect cost rates.
- Indirect cost rate caps or ranges are often based on past historical or average figure without considering future organisational plans, assuming no changes will occur in the following years.
- Inadequate calculations may lead to significant under-resourcing of key functions (management, fundraising teams) and financial strength over time (keeping reserves for at least a 6 month operational cycle).
- Despite differences between think tanks such as organisational size, geographical location, operational focus, and funding sources - funders often compare indirect rates when making budgetary decisions.
- In some cases funders expect that the contracted/grantee organisation covers indirect costs on its own.

Indirect cost rates go from 7% to 29%.

... do not correspond to think tanks' needs

- **Size does make a difference:** Think tanks' indirect rates are usually higher for smaller organisations. Indirect rates are usually inversely proportional to scale.
- **Caps and ranges are not always useful guidance:** Think tanks often struggle to identify indirect rates and are instead influenced by funders' approaches or caps on rates – even if these do not reflect their own situations.
- **Rates change over time as the organisation changes:** Important strategic choices made by the think tank may affect cost and rates over time.
 - Investments to develop or expand the capacity of current staff (fundraising, management)
 - Investments to develop new areas of work
 - Investments in new more equitable partnerships
 - Efforts to develop sufficient reserves to ensure the sustainability of the organisation
 - Provisions to allow the organisation to pursue policy influencing windows of opportunity
 - Provisions to deal with unstable economic or political context

Estimated indirect cost rates go from 18% to 51%.

Funders allowances and conditions ...

Note: In some countries think tanks are set up as for profits to avoid CSO clampdowns

Overall, allowed indirect cost rates per funder (in this sample) range from **7% to 29%**.

| Funder | Allowed indirect cost or overhead rate ^{2,3} | Conditions (if any) |
|-----------------------------|---|---|
| Packard Foundation | 15% to 25% | Depending on grantee's organisational budget (non-profit organisations) |
| Gates Foundation | 0% to 15% | Depending on type of organisation and location |
| Hewlett Foundation | Flexible, or 10% cap | Indirect rates are calculated by the grantee and dialogued based on guidelines per type of organisation. There is a 10% rate for universities. |
| MacArthur Foundation | 29% | For non-profit organisations only |
| IDRC | 0% and 13% | Only allowed for grants; consulting projects do not have a cap |
| Oak Foundation | Flexible | Flexible rate committed to fund full and fair share of indirect costs |
| USAID | 10%, NICRA, personalised | 10% rate or NICRA rate (for US based organisations). For subgrantees USAID funded projects allow to cover indirect costs based on the organisation's audited financial statements |
| Jacobs Foundation | 10% (approx.) | For non-profit and for-profit organisations |
| Stiftung Mercator | 20% (max.) | For "infrastructure costs-flat fee" – Definition requires clarification |
| Laudes Foundation | Not listed | They do fund overhead/indirect cost, but we couldn't find a specific rate |
| William T. Grant Foundation | 15% (max.) | For Major and Officer's research grants |

² Percentage of contract's value.

³ Note, in some cases this only refers to grants. Sometimes, funders treat consulting projects differently

Sources: Packard (2024), Gates (2017), Hewlett (2019), MacArthur (2019), IDRC (2024 and confirmed by P.O. in 2023), Jacobs (2023, information provided by P.O.), Oak (2023), USAID (2023, and guidelines applicable to OTT), Stiftung Mercator (2024), Laudes (2024), William T. Grant (2024), Development Initiatives and UNICEF (2023), the Bridgespan Group (2016).

... do not match think tanks' rates

- We explored indirect cost rates of think tanks and research centres from our network.
- Based on their publicly available financial statements, we estimated the indirect cost rate of each organisation. We do not recommend comparing between these organisations as the way of calculating the rates and the actual rates may vary.
- Overall, the indirect cost rate (in this sample) ranges from **18% to 51%**.

| Think tank | HQ Location & Scope of their work | Estimated indirect cost rate |
|---|-----------------------------------|------------------------------|
| PEP – a network of economic researchers | Kenya (Global) | 51% |
| Economic Research Forum – a MENA-focused research network | Egypt (MENA) | 44% |
| Southern Voice – a global network of think tanks | Peru (Global) | 35% |
| ODI – a leading UK-based international development think tank | UK (Global) | 27% |
| GDN – a large international organisation | India (Global) | 25% |
| PASGR – a pan-African research support programme | Kenya (Africa) | 25% |
| AERC – a large pan-African policy research network | Kenya (Africa) | 19% |
| CGD – a leading US-based international development think tank | US (Global) | 18% |

Sources: Calculations made based on publicly available financial statements of the listed think tanks.

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What is the effect of
this mis-match?



What is the effect of this mis-match?

- Perpetuating the idea of false efficiency that leads to a **starvation cycles**: Misrepresentation of data, unrealistic expectations, pressure to conform.
- **Distraction from think tanks' missions**: If think tanks struggle to cover their indirect costs they will concentrate their efforts towards looking for more funding rather than focusing on their mission.
- **Opaqueness**: This can lead to think tanks categorising indirect costs as direct costs to mitigate risks of not covering it; and then having to hide their practices from funders
- **Challenges for investment or strategic planning which risks sustainability**: Long term investments involve short- or medium-term changes to indirect rates.
 - SoS 2023 Results: Human resources, strategy, finance and fundraising, management-leadership.

What competencies do think tanks want to invest in?

Precisely the ones that indirect costs would cover **and are usually not allowed!**

| Desired competency | Global | Africa | Asia | South & Eastern Europe | West & Northern Europe | Latin America & the Caribbean | USA & Canada |
|---------------------------|--------|--------|------|------------------------|------------------------|-------------------------------|--------------|
| Human resources | 22% | - | ++ | - | = | - | - |
| Communications | 22% | - | -- | ++ | + | = | + |
| Strategy | 20% | - | + | = | - | + | ++ |
| Financing and fundraising | 19% | = | -- | + | = | = | - |
| Networking and engagement | 18% | + | - | = | - | + | + |
| Research capabilities | 18% | + | = | = | - | + | + |
| Management and leadership | 14% | ++ | = | - | = | - | ++ |

Note: = represents 5% or less difference from global average; + and - represent a difference of between 6% and 15% from global average; ++ and -- represents 16% or more difference from global average (source: State of the Sector Report 2023)

Source: State of the Sector Report (2023)



Recommendations



Different approaches and support

- **Change the narrative:** Organisations are different and have financial, operational, and organisational needs and expectations, each with its own strategies and planning approaches.
- **Shared understanding:**
 - Promote dialogue between the contracted/granted organisation and the project's P.O.
 - Focus on the total value of the grant/contract - are you satisfied with the expected outputs or outcomes?
 - Foster openness about the indirect cost rate of the contracted/granted organisation.
 - Seek explanations for how rates are calculated, not to compare between organizations, but to deepen your understanding and consider how your support can benefit them in the future.
- **Operational Efficiency:** Consider reducing reporting requirements to minimize operational (indirect) costs.
- Embrace **flexible and multi-year funding.**

Deep dive...

- **Change the narrative:** Organisations are different, have different financial, operational, and organisational needs and expectations, and each follow their own strategies and planning approaches.
- **Shared understanding:**
 - Promote open and honest dialogue between the contracted/grantee organisations and their programme officers/managers
 - Focus on the total value of the grant/contract (are you satisfied with the expected outputs or outcomes?) rather than on the hourly/daily cost, indirect costs, etc.
 - If you seek explanations for how rates are calculated, do not compare between organisations, but deepen your understanding and consider how your support can benefit them in the future.
- **Operational Efficiency:** Consider reducing reporting requirements to minimise operational (indirect) costs. Why not coordinate with other funders to the same organisation?

Deep dive...

- Be willing to **exclusively fund organisational strengthening or operational costs**. They exist and need to be covered for sustainability. Do not worry if your funds "subsidise" other funders who do not "pull their weight".
- Be willing to and encourage think tanks to keep **spare funds as reserves** and to use them in the future either to deal with challenging periods or organisational strengthening. Engage with them on how they plan to and use those reserves.
- Embrace flexibility and start transitioning (if you have not) into **multiyear funding**. This enables think tanks to alleviate the constant pressure of seeking funds. Thus allowing focus on their mission. Consider that indirect rates will change over time and therefore plan for increases in caps or ranges, too!
- If you still need to establish a cap or range look for multiple criteria, e.g.:
 - Size of the organisation: larger organisations can dilute costs across more projects and funders
 - Growth plans: investments in sustainability may involve higher indirect costs in the short term
 - Context: uncertain political and economic environments may demand think tanks to fund more expensive IT systems, seek contingencies for inflation, FX fluctuations and plan for unexpected costs)



Questions?





Next steps



More information

- There is a gap regarding available and updated information on the indirect cost rate policies and practices of **think tanks' funders and think tanks themselves.**
- We want to invite **funders** to provide OTT with more information about:
 - Definition and classification of direct costs and indirect costs and methodologies for calculating the indirect cost rate.
 - Indirect cost rate allowed by your organisation and conditions for it (e.g. type of contract and organisations' business model).
 - Reporting requirements on the indirect cost rate.
- We will gather equivalent information from think tanks during the State of the Sector Report 2024's survey process.

Analysis and learnings

- More data will allow us to:
 - Identify and critically assess the various practices of funders and think tanks in relation to whether they enable or challenge think tanks' sustainability.
 - Produce case studies to illustrate how funder practice can support or hinder think tanks' efforts to develop
 - Offer practical recommendations for:
 - Funders to consider (best practice note)
 - Think tanks (best practice note)
 - Members of the Funder's Circle on their own policies and related to ongoing or future grants or projects
 - The wider sector (blogs and presentations)



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