



Department  
for Education

# **Full cost recovery and rate of return**

**Managing and charging for boarding  
provision**

**January 2015**

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# Summary

## About this departmental guide

This is an operational guide from the Department for Education. This advice is non-statutory, and has been produced to help state boarding schools (SBS) understand the basic concept of full cost recovery (FCR). Reference to 'SBS' in this document means local authority maintained schools, academies and free schools.

This guide contains information on how State funded Boarding Schools (SBSs) should:

- Be calculating boarding charges on a FCR basis.
- Include a Rate of Return of 8% (**applies to academies and free schools only**) on FCR, for boarding provision.

## Expiry or review date

This guide will next be reviewed before January 2017.

## This guide is for

- Academies;
- free schools; and
- LA maintained boarding schools.

## Key points

The purpose of this guidance is to help state funded boarding schools (SBS), in setting the appropriate fees for boarding provision on a full cost recovery (FCR) basis. It sets out how crucial FCR is to the school's success, financial viability and sustainability of the boarding provision. For many SBS, calculating their boarding charges generally includes an element of direct costs and indirect costs. However, it is possible that some schools are not including all elements of indirect costs and therefore not covering and/or recovering the full cost for providing boarding provision.

Academies and free schools are classed as central government organisations for National Accounts purposes, which mean they are required to comply with HM Treasury's *Managing Public Money* (MPM) guidance.

LA maintained boarding schools remain within LA accounting boundaries.

# Section 1 – General background information

## 1.1 Introduction

It is government policy that (where possible) public sector organisations, including state funded boarding schools (SBS) should charge for publicly provided goods and services based on full economic cost. The policy set out in this guidance is based on the Fees, Charges and Levies guidance, under [Chapter 6 of HM Treasury's Managing Public Money](#) (MPM).

## 1.2 Basic policy

Boarding provision is classed as 'discretionary services', which means SBS can charge for boarding provision and calculate the fees to be charged as set out in [Annex 6.1 of MPM](#). This explains that, public sector organisations, including SBS, should not subsidise the cost of goods and services sold into competitive markets and should aim to recover full costs, plus a real rate of return.

SBS, including academies and free schools are **not** allowed to charge fees for education provision.

The implementation of a Rate of Return of 8% by academies and free schools should be as soon as reasonably possible, which means its full implementation will not be effective across the sector, in recognition of the variable circumstances that may apply to individual academies and free schools.

Applying a rate of return **is not** a requirement for local authority (LA) maintained boarding schools as they are prohibited by Section 458 of the Education Act 1996, from charging above full cost for boarding provision. However, LA maintained boarding schools should be charging for boarding provision on a full cost recovery basis, for which indirect and overheads costs should be included.

If you are a LA maintained boarding school with an Academy Order or is thinking about applying to become an academy, you will be required to set out, in any consultation about academy status, the requirement to charge a rate of return of 8% and the potential impact on boarding fees.

Any gains from boarding activities must be invested back into the boarding provision. It can for example be used to finance boarding hardship bursaries scheme or related boarding capital investments.

### **1.3 Setting the charge**

The concept of full cost recovery (FCR) represents the best value for money for the state funded boarding schools (SBS). There may be potential risks to the school's success, financial viability and sustainability if FCR is not properly applied. Whilst there may also be additional administrative and budgetary responsibilities for the school, in relation to the recovery of any charges, these should be covered in the full costs calculation and should not be a determinant for not charging the full fee.

It is a requirement for academies and free schools to charge for boarding provision on a full cost recovery basis and must apply a Rate of Return (RoR) of 8% on boarding charges.

A rate of return can be applied to other discretionary services; however, there may be Tax and/or VAT implications for non-boarding activities. Please seek further advice from your local [HMRC](#) Office / Tax advisers.

### **1.4 Tax and VAT implications**

HMRC has confirmed that boarding fees will continue to be treated as a non-business activity on which VAT would not be chargeable, even with the application of FCR plus a 'rate of return', provided the boarders receive boarding and education provision. For example, the fee to be charged for the letting of rooms would be on a full cost recovery basis, plus the 8% rate of return, thereby maximising the income generation from room letting.

However, the letting of boarding accommodation and facilities during holiday period is deemed to be a business activity on which VAT would be chargeable to the recipient (although there is a rule which allows the charge for sleeping accommodation to be relieved from VAT when a guest stays for over 28 consecutive days or more).

The VAT arrangements for boarding provision is very complex and incorrect application could result in a fine and/or penalty charge by HMRC therefore the School should seek advice from its local HMRC Office/Tax advisers to determine any Tax and/or VAT implications on boarding provision, to ensure correct treatments are applied as appropriate.

Additional information and guidance on what is considered a business activity and/or non-business activity is available on [HMRC](#) website.

### **1.5 Financial accountability and reporting**

LA maintained boarding schools are accountable to their relevant local authority, foundation trust/governing bodies. Academies and free schools are accountable to their

academy trust, multi-academy trust, governing body and/or Education Funding Agency (EFA), on how much they have decided to charge for boarding provision.

State funded boarding schools (SBS) must ensure all relevant boarding incomes and expenditures are included in their annual reports / accounts, in accordance with the accounts direction issued to the SBS by the relevant local authority and/or EFA.

If you are unsure about what to include in your annual reports / accounts: LA maintained boarding schools should seek further advice from their local authority; and academies and free schools should contact the [Education Funding Agency](#).

## Section 2 – Full cost recovery

### 2.1 The importance of full cost recovery

Full cost recovery means ensuring your organisation recovers the full cost of delivering a service, product or project, including the relevant proportion of your organisation's overhead costs.

It works on the premise that both direct costs and a relevant portion of overheads (indirect costs) costs are integral to the support and delivery of a service, product or project and **must** be included when calculating the overall cost of a service, product or project.

It is important for your school's success and financial viability. If you are not recovering the full costs of delivering your boarding provision, you could be creating a financial shortfall for your school thus affecting your school's success and financial viability and the services you provide. This shortfall may have to be met by you through additional fundraising activities or other means.

### 2.2 Costs associated with delivering boarding activities

There are normally two types of costs (i.e. direct costs and Overheads costs) associated with delivering boarding activities or services within your school:

- **Direct costs** - are incurred as a direct result of delivering boarding activities.
- **Overhead costs** (or indirect costs) are those needed to support and administer the school and its activities. These costs are sometimes also referred to as 'back office' costs (i.e. management / administration support) and can be split between various activities within the school.

It is for the academy/free school trusts to determine what element of fixed and indirect costs actually relate and are apportioned to the boarding provision. Therefore some academies and free schools with boarding should take this opportunity to review and adjust such costs to reflect the changing profile (of consumption) of the boarding provision over time.

### 2.3 Costs to be included in calculating boarding fees

Here are some examples of associated costs in terms of delivering boarding provision:

- Direct costs are:
  - Accommodation costs (purchasing, leasing premises)

- Fixture and fittings
- Lighting
- Heating
- Boarding building maintenance
- Cleaner costs
- Security costs
- Dedicated staff salaries to boarding provision only
- Overheads (indirect) costs are:
  - Human Resources (administering of staff, payroll, recruitment).
  - Finance (accounting, budgeting, invoicing, purchasing, depreciation, and cost of provisions, insurance).
  - Procurement/Facilities (purchasing, maintaining leasing, office material and equipment such as photocopiers).
  - General admin tasks (such as answering telephones, data processing)
  - Staff salaries (covering more than one function).

**Note:** the above lists of examples are not exhaustive.

## 2.4 Benefits of full cost recovery

By implementing full cost recovery you are ensuring that your boarding provision is fully funded and sustainable. Calculating the full economic costs will help you to decide whether or not to provide boarding activities or services. If you are an academy or a free school you must apply a Rate of Return (RoR). See **Section 3** for more information on how to calculate FCR and RoR.

It is also beneficial to your school if you are:

- seeking grant funding - you will know the exact amount you need to ask for;
- applying to deliver boarding provision or other services for which there is a defined price – you can compare the funds available with your full costs of delivering boarding or other services; and

- in a competitive bidding situation - it will help you decide if you want to bid and at what level.

## 2.5 Identifying direct and indirect costs

**Direct costs** - in most cases, it is generally easy to identify accurately the costs of delivering boarding provision or services. For example, the costs of beds could be directly attributable to boarding. For some direct costs such as utilities you may need to apportion the cost where buildings are shared.

**Indirect (overheads) costs** – these are less clear to identify. Once you have identified an overhead, you need to determine the appropriate basis for distributing the costs across your specific boarding activities or services. This process of sharing out the overhead costs is called 'overhead absorption' or 'overhead recovery'.

## 2.6 Apportionment of direct and indirect costs

There are a number of bases for apportionment of direct and indirect (overheads) costs that could be applied to boarding provision or services. You should document which method you will adopt to ensure your calculation is consistent year on year.

For example:

- usage – expenditure incurred directly in undertaking boarding activity;
- per capita – the number of people employed within the boarding activity compared to the overall total;
- space - floor area occupied/used for the boarding activity compared to the overall total;
- time – the proportion of time spent on the boarding activity compared to their total time where the staff duties are multi-activities – e.g. education, pastoral, boarding activities etc.

## 2.7 How to calculate full cost recovery

To calculate the full costs of your provision or service, you need to:

- calculate the direct costs of the boarding provision or service;
- calculate the total overhead costs for the whole organisation; and
- allocate a relevant share of overhead costs to the boarding provision or service or project.

In order to ensure full cost recovery (FCR) for your boarding provision or services to be provided, you need to complete a two-step process:

- **Identify and account for all costs** – ensure that no costs are omitted and that you have appropriate information e.g. budgets and forecasts, with which to cost the boarding provision or service.
- **Allocate costs** – ensure that you allocate all direct costs and a relevant share of overhead (indirect) costs to the boarding provision or service to be provided.

You should have a robust financial reporting and accounting systems in place that you can use to allocate costs on a monthly basis for the boarding provision.

## 2.8 Implications of not calculating FCR properly

- If you under recover your costs, it will affect the financial viability and sustainability of the school and ultimately its success. Therefore it is not a good idea to wait until the boarding activity has started or year end, to assign all costs as it may either be too late to recover costs or time consuming to start allocating costs.
- The Office of National Statistics normally classifies charges higher than the cost of provision, or not clearly related to a service to the charge payer, as taxes. Such charges always require explicit Ministerial decision as well as specific statutory authority.

It is good practise to review these costs at least yearly so that charges to the public for your boarding provision, other services or products are also reviewed and consistent with the full cost recovery concept as your costs are likely to go up due to inflation and/or other resources/economic factors. Your apportionment assumptions should remain consistent.

## Section 3 - Charging full costs, plus a rate of return

**Note:** this section applies to academies and free schools

### 3.1 Definition of a rate of return

A rate of return (RoR) is the ratio of money gained or lost on an investment relative to the money invested and it is often expressed as a percentage.

### 3.2 Applying an appropriate RoR for boarding provision

HM Treasury and the department have agreed an appropriate rate of return (RoR) to be applied by academies and free schools for boarding provision. The agreed RoR is set at 8% maximum as it was considered to be an average representation, which is appropriate for the academies and free schools sector. The 8% RoR must be applied by all boarding academies and free schools in accordance with the *Fees, Charges and Levies* guidance, under [Chapter 6 of HM Treasury's \*Managing Public Money\*](#)

Please see **Section 4** for examples of how FCR, including a RoR for boarding provision is calculated.

### 3.3 What application of RoR means in reality

The Department for Education (the department) recognises that the actual picture in terms of the boarding fees calculation is less clear and accepts that the true nature of the boarding fees calculation is uncertain in terms of whether full cost recovery in respect of boarding has been fully applied by the sector. However, it is for the academy and free school trusts to ensure that relevant element of fixed and indirect costs that relate are properly apportioned to the boarding provision.

### 3.4 Charging above cost for discretionary services

Academies and free schools can charge above cost for boarding and/or other discretionary services. This is explained in Chapter 6 of HM Treasury's [Managing Public Money](#) (MPM) guidance. It states that there are exceptions to full cost charging for certain discretionary services provided in competition with the private sector, where a rate of return is normally charged.

As such boarding activities provided by academies and free schools qualify as an exception hence you must apply a rate of return of 8% to calculate the fees to charge the public for such services.

### **3.5 Ability to offer bursaries**

The academy and/or free school trust can continue to work with its partners to provide bursary funded boarding provision to pupils. All boarding provision should be charged at the same fee rate but the bursaries can be used to reduce the boarding fees that parents and/or carers pay.

The income generated by applying a rate of return can also be used to fund hardship bursaries to pupils.

### **3.6 Restrictions on the use of gains**

Gains resulting from the application of the 8% RoR for boarding activities **cannot** be used for non-boarding activities.

### **3.7 Change or review of the rate of return**

The rate of return will change over time once the department is content that it has been adopted across the academy and free school sector. The 8% RoR percentage will be reviewed annually.

## Section 4 – Examples of FCR and RoR calculations

### 4.1 Example 1 - Apportioning direct costs

A Trust is providing boarding and education to pupils at the school premises. No other services are run from the premises. The services provided operate from distinct and separate parts of the same building so direct costs are easily identifiable and include building, maintenance, furniture, fixtures and fittings etc. from the boarding half of the building. Boarding and education share the same electricity supply and pastoral staff equally.

Direct costs	£
Direct costs for boarding provision (building costs, maintenance etc.)	50,000
Total Electricity bill = £1,000 apportioned on a 50/50 split so boarding cost =	500
Pastoral staff total cost = £25,000 apportioned on a 50/50 basis so boarding cost =	12,500
Boarding provision costs	63,000

Therefore the direct costs of the boarding provision has been identified as **£63,000**

### 4.2 Example 2 - Full cost recovery calculation

Using the same Trust as above we also have the following information: The Board of trustees/governors spend 30% of their time on boarding governance and strategic development:

- Boarding occupies 15% of the Director (or equivalent)'s time;
- Book-Keeper, Receptionist and general office administrator staff etc. who deal with queries across the whole school/academy. A decision is taken to apportion their costs based on the proportion of direct costs for boarding compared to the total direct costs for the whole school/academy. This works out at 25% boarding, 75% education provision.
- Office consumables – e.g. office paper, pens etc. which cannot be attributed specifically to either provision. Apportionment used the same basis as for administrative staff above.

- All other overheads to be apportioned on the basis of floor space occupied which is a 50/50 split.

They all occupy parts of the same building as the academy/free school; therefore the costs for the additional items are as follows:

Total cost	£
Board of trustees/Governors	2,000
Director (including cost of NIC and pensions)	40,000
Book-Keeper and Administrative staff	27,000
Office Consumables	3,000
All other overheads	75,000

Using FCR model

**Step 1** - Calculate direct costs - this has been identified as **£63,000** - see example 1 above. **Step 2** - Calculate indirect (overheads) costs:

Cost	Boarding	Education	Total
Board of Trustees/Governors (30% boarding)	600	1,400	2,000
Director (15% boarding)	6,000	34,000	40,000
Book-keeper and administrative staff (25% boarding)	6,750	20,250	27,000
Office consumables(25% boarding)	750	2,250	3,000
All other overheads (50/50 split)	37,500	37,500	75,000
Total indirect costs	51,600	95,400	147,000

**Step 3** - Calculate the total cost for the boarding provision:

Cost	£
Direct cost (from example 1 above)	63,000

Cost	£
Indirect cost (from step 2 above)	51,600
Total cost of boarding provision	114,600

**Step 4** - To calculate the base boarding fee you should now divide the total boarding cost by the number of boarding places in the academy or free school. In this example there are 50 boarding places so the basic fee would be:  $\text{£}114,600 \div 50 = \text{£}2,292$

### 4.3 Example 3 – Rate of return

Using the figures from Example 2 above we can calculate the full fee that can be charged by an academy or free school as follows:

Cost	£
Basic boarding fee per place	2,292.00
Rate of return ( $\text{£}2,292 * 8\%$ ) =	183.36
Total FCR & RoR fee per boarding place	2,475.36

## Section 5 - Sources of information

[Department for Education](#) – is responsible for education and children's services in England.

[Education Funding Agency](#) - provides revenue and capital funding for education for learners between the ages of 3 and 19, or the ages of 3 and 25 for those with learning difficulties and disabilities. It also supports the delivery of building and maintenance programmes for schools, academies, Free Schools and sixth-form colleges.

[Funding Central](#) – is a free resource for charities, voluntary organisations and social enterprises. It provides information on financial management, funding and finance opportunities.

[Charity Commission](#) - the regulator for charities in England and Wales.



Department  
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