Advantages and Disadvantages of Chargeback and Allocation Funding Models

Speaker: Rena DeLevie, Consultant, Cella

Common Funding Models for In-House Creative Services Groups

1. **Chargeback Model:** Department must recover all expenses through an hourly or project-based chargeback system so that when the fiscal year concludes the total expenses roughly (or in some cases, exactly) equal the total revenue (chargebacks). Clients (internal customers) are charged based on actual usage of the department's services.

2. **Allocation Model:** Department is funded centrally through a per FTE cost to all business units; business units are charged regardless of volume of use. This funding model is common to other non-revenue generating shared services departments such as IT, mail services, facilities, procurement, etc.

3. **Hybrid Model:** Department must recover a portion of its expenses through a chargeback system; the remaining costs are allocated through a per FTE cost to all business units.

Pros and Cons of the Funding Models

	CHARGEBACK MODEL	ALLOCATION MODEL
PROs		
CONs		

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Typical Expenses of an In-House Creative Services Team

1. **Personnel Expenses**
   - Employee Salaries
   - Benefits, Taxes, Social Security, 401K Matching
   - Overtime / Bonuses
   - Other Incentives (e.g., gift cards)
   - Temporary Staffing

2. **Direct Operating Expenses**
   - Travel and Entertainment
     - Airfare, hotel, meals for conferences and other travel
     - Team lunches / dinners
     - Team outings / events
   - Training
     - Conferences
     - Lynda.com
   - Consulting
   - Hardware / Software
     - Computer upgrades
     - Adobe and other vendor software updates
     - New software
     - New or replacement accessories (mice, keyboards, etc.)
     - Digital Assessment Management system
     - Workflow/project management solutions
     - Annual fees for in-place software and other IT solutions
   - Misc
     - Smart Phone reimbursements
     - Stock Photography
     - Shipping
     - Agency Fees

3. **Overhead**
   This figure is generally provided by your Finance department and is typically a "per FTE cost"
   - Shared Services fees
     (IT, facilities, procurement, legal, other corporate administrative functions)
   - Rent
   - Utilities (water, electricity, etc)
   - Etc.

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Determining a Chargeback Rate

This is a simple hourly chargeback rate calculation model that assumes a department will charge a blended rate (one rate) across all roles and services—which may or may not be the case for your department. If you plan to charge multiple rates, this calculation can be adapted, although there are several criteria you will need to consider in advance, e.g., how to allocate department overhead costs such as admin and manager salaries across the varied rates. Cella recommends a more in-depth process for determining multiple rates than this calculation offers. That said, this simple calculation is very helpful in determining a blended hourly billing rate.

1. Determine Department Capacity

Enter the number of days the average department employee receives in the form of paid time off (include vacation, sick, personal leave, etc.).

Enter the number of corporate holidays observed by your company.

For each position in your department, identify a billing expectation*. Then identify the total number of staff members in each of the roles you listed to the left.

Total available billable* hours per employee (before OT)

Department capacity can be calculated now by multiplying the billable hours per role by the number of employees in each role and adding the totals.

PART ONE

Hours	# of Days	Time
2080	260	Number of Business Hours per Year
-160	20	Average Paid Time Off per Employee (Vacation, Sick, etc)
-72	9	Number of Company Holidays
1848	231	Capacity/Staff Member

Total available business hours per employee (before OT)

PART TWO

Billable Expectation Hours	Percentage	Roles	# of Employees in These Roles
1663	90%		0
1571	85%	Designers, Editors	12
1478	80%		1
1386	75%		0
1294	70%	Account Managers	2
1201	65%		0
1109	60%	Creative Director	1
924	50%		0
739	40%	First-Level Managers	2
554	30%		0
370	20%		0
185	10%		0
0	0%	Admin, Department Head, Traffic Manager	3
		Total Team Members	21
		Total Annual Department Capacity	38808
		Total **Annual** Department Billable Capacity	25502.4
		Avg. Total **Monthly** Department Billable Capacity	2125.2
		Avg. Total **Weekly** Department Billable Capacity	490.4
		Average Department Billing Rate	*66%*

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* Billable rate is also referred to as utilization or productivity rate. Activities that are considered billable or "productive" are those which are related to clients' projects; this includes project meetings, email/phone/in-person communications, project management activities, design, editing, and the like. Many departments also bill for account management activities.

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Determining a Chargeback Rate (continued)

2. Calculate the Hourly Chargeback Rate

Refer to your department budget to identify the budgeted amount per line item. If a line item in your budget is not included here, be sure to still include that cost. Only include the expenses you are required to recover. Seek your Finance partner's input as necessary.

Don't forget to include any agency fees or temporary/contract/freelance staff costs that are paid through your budget and not recovered by other means from your clients.

PART ONE: Personnel and Labor-Related Expenses	
Expense	Annual Cost/Budget
Employee Salaries	
Benefits, Taxes, Social Security, etc.	
Overtime/Bonuses	
Temporary Staffing	
Agency Expenses	
Other 1	
Other 2	
SUM	$ -

PART TWO: Direct Expenses	
Expense	Annual Cost/Budget
Travel & Entertainment	
Training	
Consulting	
IT Costs	
Agency Fees	
Other 1	
Other 2	
Other 3	
Other 4	
SUM	$ -

PART THREE: Allocated Expenses	
Expense	Annual Cost/Budget
Overhead	
Other 1	
Other 2	
SUM	$ -

Total Department Expenses	$ -
Annual Billable Capacity	25,502
AVG. HOURLY CHARGEBACK RATE	$ -

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Sum of all three expense types

Sum of annual capacity from previous "department capacity" calculation

Total Department Expenses divided by Annual Billable Capacity = Hourly Chargeback Rate

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