Project Cost of Internal Resources

Neville Turbit

Overview

The issue of whether internal resources should be costed in projects has been around since projects began. If a person is seconded from their normal role, either part time or full time to a project, should their costs be borne by the project or should they be treated as a free resource. There is no right answer, and different organisations treat the situation differently. This white paper investigates a few of the questions around the issue.

An Internal Project Resource Example

Let us imagine that Bill Jones is normally the manager of the production department. He is suddenly dragged into a project for 50% of his time. There are three options:

- Bill works longer hours. Instead of an 8 hour day he works 12 hours
- Bill delegates part of his production management role
- Bill works harder and manages to cover both jobs in something less than 12 hours

Each of the options has a financial implication on the organisation.

Working Longer Hours

If he works longer hours for an extended period, productivity will start to slip. People working 50% extra time usually show signs of burn out after a month or two. It becomes a spiral. Bill becomes less productive and consequently has to work longer hours to get the job done. This of course leads to another drop in productivity, and so the spiral continues.

Eventually, mistakes are made, and Bill decides it is all too much and leaves the organisation. Both the project and the production department suffer. Someone else comes on board and tries to pick up the loose ends but of course it was all unravelling in the last few weeks Bill was around.

The "free" resource suddenly gets very expensive. It might even lead to an external resource being added to the project and an unexpected cost is incurred. So, if it is valid to add the external resource cost to the project, why was it not valid to add the internal resource that was doing the same job?

Delegation

If Bill decides to delegate part of his role, it is just spreading the pain. Instead of one person working 4 hours extra, perhaps 4 people work an hour extra. If the people are paid on an hourly rate, it becomes an additional cost to the organisation. If they are on a flat salary, the issue of where the cost should be borne is less clear.

Working Harder

Perhaps this should be split into two options. Working harder may mean working more efficiently. In that case, we have to ask why Bill was not working more efficiently before. If he had been more efficient, should the organisation have costed his Production Manager role as, for example, an 80% resource? Should he have been 4 days per week running Production, and have another role for 1 day? Was his job overstated? The costing problem is not only with the project. It is with the way the Production Department is funded.

The second option is that he does not do his job in Production as diligently as before. He glosses over reports, and management issues. In this case there is a loss of quality in how he does his work. The question then becomes one of the organisation accepting a short term quality fall in the management of Production, to enable Bill to participate in the project. The financial implication is that Production is paying the same amount for a lower quality management effort.

Financial Implications

All of the above illustrate that you can't get something for nothing. By using internal resources, there is always a financial implication. It may be that Production pay the same for less. It may be that they incur a cost of replacing a person either on a temporary basis, or permanent if the person resigns. It may be that they were paying an amount for someone who was working at a lower productive level than they should have been. If there is a cost – either directly or indirectly - to the organisation from the project, where should the cost lie? I would suggest the project.

Cost Benefit

Another aspect is the issue of project cost justification. Typically a business case contains every last benefit. Every cent that can be identified as a potential saving is included. If internal costs are not included however, how realistic is the business case?

I have seen projects that were marginal on a cost benefit case, not include internal costs. If they had been included, the project would clearly make no sense. It was argued that we paid for these people anyway so why include them in a calculation? The answer is because somewhere along the food chain something will suffer, and there will be a cost implication.

To turn the argument around with our example above, if, regardless of the project, Bill were to only work and be paid for 4 days a week, the organisation would take that as a 20% cost saving. They might even decide that he was not needed for a full 5 days. On the other hand, they might decide they would accept a lower quality of management and pay less. An efficiency gain. Why should the Production department not reduce the cost allocated to Bill by one day, and charge one day to the project if the project triggers this efficiency gain?

Project Funding versus Project Cost

The typical reason for not including internal resources is that people confuse project cost and project funding. Funding is the money allocated by the company to undertake the project. Cost is the real cost of undertaking the project. If you need funding, but internal resources are considered free, then your focus is on the $X additional money you need to complete the project. If you want to see if the project is viable, you need to look at total cost including internal resources.

Extended use of Internal Resources

Once allocated to a project, the shrewd project manager will try and get as much done with free resources, and as little done with paid resources as possible. If the estimate of man days to complete the project proves to be too low, let us try and get the extra hours taken up by free resources. If all resources were costed, there would be a bigger drive to use the most appropriate resources. This may mean that the internal resources did not get sucked deeper into the project to the detriment of their day jobs.

A Proposed Solution

My recommendation to organisations that do not cost internal resources is that they run two sets of books. By all means, don't charge the resources to the project, but track the proportion of the time they are spending on the project. Calculate a rate based on the total cost of the employee and use that as a basis for cost justification of the project. Use it for reporting purposes to track the"real" estimated and actual costs. In this way, management is aware of the true cost of the project rather than just what is reflected in the accounts. The implication is that timesheets must be maintained by all resources.

Conclusion

How to treat internal resources from a financial viewpoint was, is and will be a contentious issue. The one key thing to remember is the difference between costing and funding. If the objective is to cost justify the project, internal resources must be included. If the objective is to obtain money to do the project, then it is not as important to include internal resources. Whichever way your organisation operates remember, there is no free lunch.

Neville Turbit has had over 15 years experience as an IT consultant and almost an equal time working in Business. He is the principal of Project Perfect. Project Perfect is a project management software consulting and training organisation based in Sydney Australia. Their focus is to provide creative yet pragmatic solutions to Project Management issues.

Project Perfect sell "Project Administrator" software, which is a tool to assist organisations better manage project risks, issues, budgets, scope, documentation planning and scheduling. They also created a technique for gathering requirements called "Method H"™, and sell software to support the technique. For more information on Project tools or Project Management visit www.projectperfect.com.au