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POLICY

FINANCIAL, BUDGETARY AND ADMINISTRATIVE MATTERS

Agency support costs

Operational activities for development: Project support costs

Report of the Administrator

SUMMARY

The present report is submitted to the Governing Council pursuant to General Assembly resolution 42/196 of 11 December 1987 on operational activities for development, in section V, paragraph 34 of which, the Governing Council is invited, given the expiry in 1991 of current arrangements for project support costs, to begin considering successor arrangements. The report provides a historical brief on the subject-matter and includes the Administrator's suggestion concerning a future course of action which the Council may wish to take.

1. The General Assembly, in section V, paragraph 34, of resolution 42/196 of 11 December 1987, invited the Governing Council of the United Nations Development Programme (UNDP) to begin consideration of successor arrangements to those contained in Governing Council decision 80/44 of June 1980 for project support costs which would become effective as from 1992.
2. The present is intended to provide the current membership of the Governing Council with a brief history of the subject of programme support costs, which is a reflection of the time and effort devoted by many to the question of overhead costs.
3. The issue of overhead costs incurred in the carrying out by the United Nations system organizations of extrabudgetary operational programmes such as those funded by UNDP and the sharing of these costs has for more than 30 years engaged the attention of the Governing Council, the Economic and Social Council, the Advisory Committee on Administrative and Budgetary Questions (ACABQ), the legislative and governing bodies of the executing agencies and the Joint Inspection Unit (JIU).
4. While Economic and Social Council resolution 222 (IX) of 15 August 1949 and General Assembly resolution 1240 (XIII) of 14 October 1958, establishing the Expanded Programme of Technical Assistance (EPTA) and the Special Fund, respectively, did not carry definitions of overhead costs, the term came to be applied to those costs incurred by the participating organizations in the implementation of projects financed from extrabudgetary funds i.e., administrative and operational services costs for EPTA; overhead for the Special Fund and, later on, programme or project support costs for the merged activities.
5. Throughout the 1950s, discussions and deliberations on the subject of overhead reimbursement took place. In the establishment of the Special Fund, the General Assembly, by its resolution 1240 (XIII), specifically decided that the principle of reimbursing only clearly identifiable additional expenses should apply.
6. With respect to EPTA activities, ACABQ: (a) suggested in 1954 that administrative and operational services costs should not exceed 12 to 14 per cent of the total programme costs incurred by participating agencies; (b) suggested in 1958 the consolidation of overhead in the regular budgets of the participating organizations, together with a lump-sum budgetary credit from the EPTA account if that account was to continue to meet a part of the overhead; and (c) recognized in 1959 that assumption of overhead costs by regular budgets without any credits from the extrabudgetary accounts was not solely a budgetary technique but that such action would require a decision of policy to be taken by Governments. In the absence of such a decision, ACABQ suggested a lump-sum payment of 12 per cent of project costs incurred for the preceding biennium.
7. The Economic and Social Council adopted, with some modification, the 12 per cent figure in its resolution 737 (XXVII) of 30 July 1959, which remained substantially in effect until 1965.
8. The Governing Council of the Special Fund continued to review progress reports on the subject of overheads submitted by the Managing Director, and between 1959 and 1969 there emerged a pattern of reimbursement which separated the costs related

to equipment from the costs related to other objects of expenditure. With effect from 1965, a reimbursement rate of 3 per cent for the cost of equipment and supplies and 11 per cent for other project costs was established.

9. Therefore, in 1965 the provisional reimbursement formulae were:

EPTA: 12 per cent of project costs of the preceding biennium;

Special Fund: 3 per cent of the purchase cost of equipment and supplies and 11 per cent of other project costs.

10. In 1965, ACABQ maintained its view that the basic concept that the technical assistance programmes should be debited only with additional administrative costs occasioned by them is still valid. It noted, however, the difficulty of identifying these costs. The Committee felt that the basic principle that the organizations should continue to provide from within their regular budgets for a substantial portion of the overhead costs of the extrabudgetary programmes remained valid.

11. Following on ACABQ recommendations, the Governing Council authorized a reimbursement rate for EPTA projects at 14 per cent and for Special Fund projects at a flat 11 per cent of total project costs. These rates remained in effect until 1 January 1972 when, as a result of the consolidation of EPTA and the Special Fund into UNDP, a single provisional rate of 13 per cent of the costs of all UNDP projects was established for the year 1972-1973. A provisional revision of the rate to 14 per cent for the years 1974-1977 was approved by the Governing Council at its nineteenth session in January 1975.

12. As these changes in reimbursement rates developed over the years, there was the ever-present feeling that both the methods used to determine the rates and the results obtained were rather arbitrary in nature. Various attempts were made to quantify rates in a more scientific matter. In 1969, the Joint Inspection Unit (JIU) came to the conclusion in its report (JIU/Rep/69/2) that arriving at an average rate to be used for overhead costs reimbursement would require the introduction of an itemized cost accounting system or some other system of measurement which would provide the necessary data.

13. This report was followed by the undertaking in 1971 of a special study group, with the World Health Organization (WHO) and the United Nations Educational Scientific and Cultural Organization (UNESCO) participating, which received the full support of UNDP.

14. In 1972, a Consultative Committee on Administrative Questions (CCAQ) Inter-Agency Task Force was created under the auspices of the Administrative Committee on Co-ordination (ACC). Its task was to develop and introduce a general cost measurement system to be used in helping to arrive at management decisions and for cost control purposes. It was believed that the system could also contribute towards a solution of the vexing problem of determining appropriate percentages for application to overhead cost reimbursements. In the area of operational activities, it defined the major elements of support costs, both technical and

non-technical, and developed measuring devices for each of the elements. The average cost of technical and non-technical support to UNDP-financed projects was found to be 23.3 per cent, thereby establishing that agency resources expended in support of projects exceeded by a substantial margin the amount reimbursed by UNDP.

15. JIU returned to the overhead question in late 1972 at the request of the Administrator and in its report entitled "The introduction of cost accounting in the organizations of the United Nations Family" (JIU/Rep/72/10) provided comments on the reports of the CCAQ Task Force. The JIU expanded upon the view initially expressed in its 1969 report that the only way to arrive at a reliable cost measurement procedure was to apply uniform cost accounting throughout the United Nations system.

16. The CCAQ Task Force report with the results of 1973 agency applications of the cost measurement system, together with comments from ACABQ, JIU and the Food and Agriculture Organization of the United Nations (FAO), was submitted to the Governing Council at its nineteenth session in 1975 (DP/77 and Add.1-5).

17. As previously stated, the Governing Council, presumably guided by the results of the cost measurement study, found it in order to increase the rate of reimbursement of overhead costs to 14 per cent for the period 1974-1977. At that time, too, the Governing Council approved the application of a related flexibility provision for smaller agencies which enabled the Administrator to negotiate additional lump-sum overhead reimbursements for those agencies.

18. At its twenty-fourth session (1977), the Governing Council decided to continue the 14 per cent reimbursement rate for 1978-1979. By decision 79/40 of 2 July 1979, the Council agreed that this same arrangement should obtain through 1981. Also in response to Council decision 79/40, the Administrator appointed a consultant on the support costs issue; the report resulting from the study (DP/WGOC/31) was submitted in early June 1980 to the Inter-Governmental Working Group on Support Costs of the Governing Council. At its fifth session in June 1980, the Working Group, having considered the Rhodes Study, formulated its decision on the support costs question (DP/WGOC/32/Add.1) which it recommended for adoption by the Governing Council. The Governing Council, taking note of the report of the Inter-Governmental Working Group on Support Costs, in decision 80/44 of 27 June 1980 set out a series of arrangements for "reimbursement by UNDP of agency support costs for operational activities in respect of the financial years 1982 to 1991. The basic authorized reimbursement rate was 13 per cent of annual project expenditures. Additionally, agencies were requested to submit annual reports on an ex post facto basis, indicating the elements of support costs incurred by them in the preceding year in the execution of operational activities for development.

19. Over the years, a number of proposals have been advanced for the modification of the reimbursement system. Among these alternative approaches to the practice of applying a straight percentage of operational expenditures were: (a) inclusion of overheads in the regular budgets of the agencies; (b) arrangements to support an agreed infrastructure level in each agency; and (c) inclusion of overhead in individual project budgets. None of the above options were found acceptable to all

interested parties for a variety of reasons. It should be recalled that whenever changes were put forward, ACABQ, in its comments thereon, expressed its support for the idea that the relationship between the executing and funding agencies was to be one of partnership. ACABQ maintained that the executing agencies were not mere contractors delivering services on the basis of full reimbursement. On the other hand, the funding agencies could not assume that the executing agencies would be prepared automatically to bear any extra cost of the services they provided in support of technical co-operation programmes. ACABQ also agreed with the view of the Secretary-General that no satisfactory formula for support cost reimbursement had resulted from the various technical studies, cost measurement exercises or other mathematical calculations and that any determination of the level of reimbursement would involve the employment of political judgement by the Member States. ACABQ was also of the opinion, shared by JIU, that the degree of support by executing agencies to operational activities financed from voluntary funds was a matter for the legislative organs of those agencies to decide and therefore any recommendation to modify any existing reimbursement arrangement would require consideration of the positions taken by executing agencies.

20. As to the immediate future, the Administrator believes that, in considering their approaches to resolving the question of project support costs, UNDP and other organizations and bodies may, understandably, be occupied by thoughts such as those expressed in the consultant's report (DP/WGOC/31) that in the last 30 years tens of millions of dollars must have been spent and countless words have been written in a vain search for an ideal solution to the problem of establishing and apportioning support costs and that would be inexcusable if yet more money and energies were diverted from the course of development to which, in all conscience, they should be devoted.

21. Bearing in mind, however, the historical background and the very complex nature and political implications of the issues involved, the Administrator suggests to the Council that it consider once more the possibility of establishing an intergovernmental working group to deal with the matter adequately.

22. As to the timing of a review by such a working group, it is important that its findings are available by, or preferably before, June 1990, since the framework for the fifth programming cycle is scheduled to be finalized by that same date. It may therefore be necessary to convene inter-sessional meetings of the group, as appropriate.

23. The Administrator further believes that the working group might function more effectively if its size were limited to three representatives from each geographic region. Additionally, since the financing of project support costs has always been and is likely to continue to be shared between the voluntary contributions to UNDP and the regular budgets of the executing agencies, it would, in the opinion of the Administrator, also be advisable to include three representatives from among the governing bodies of the agencies.

