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AGENCY SUPPORT COSTS SYSTEM

I. PURPOSE

1. Following a review of this subject at the second regular session 1996, the Executive Board in its decision 96/23 requested the Administrator to prepare a conference room paper on the agency support costs system and decided to consider, at the annual session 1996, the proposals contained in documents DP/1996/13 and DP/1995/49, and the additional information provided.
2. Document DP/1995/49, originally prepared for the third regular session 1995, reports on the financial status of the agency support costs system that was introduced in the fifth programming cycle (1992-1996) under decision 91/32. DP/1996/13 outlines possible modifications to the operation of the current agency support costs system taking into account: fifth cycle experience; the simplified system of support cost earmarkings approved in the successor arrangements for UNDP programming (decision 95/23); and the overall procedures being established for implementation of these arrangements.
3. In response to the request for additional information, section II of this conference room paper outlines some of the key conceptual underpinnings of the agency support cost system as it has developed over the past 25 years. This section also provides an overview of the operational elements of the current support costs system introduced in the fifth cycle, and the consolidated financial earmarkings introduced under the successor programming arrangements. Section III clarifies and elaborates the modifications suggested by the Administrator in DP/1995/49. To facilitate consideration of the subject at the annual session 1996, section III also provides additional information on the advantages and disadvantages of possible approaches to increase openness and competitiveness in the procurement of technical services.

II. EVOLUTION OF THE AGENCY SUPPORT COSTS SYSTEM

1. Origin of the support costs concept

4. The term "agency support costs" risks being interpreted too narrowly as applying solely to specific financial facilities. In reality, support cost arrangements should be seen as a reflection of the basic roles ascribed to UNDP, Government and the United Nations specialized agencies under the tripartite partnership created for the programming and delivery of UNDP-financed development cooperation. Thus, changes to the support costs system over time not only affect financial arrangements, but also represent basic transformations in the roles of the development partners.

5. The "Consensus" decision of 1970, which can be seen as a constitutional foundation for UNDP, envisaged a tripartite partnership among Governments, UNDP and specialized agencies that would help translate development programmes into realities. This partnership recognized that the United Nations agencies, some of which predate the United Nations itself, embody considerable technical and sectoral expertise relevant to the needs of developing countries. Not only would the technical expertise of agencies enrich the quality and content of development programmes, but practical feedback from project involvement would provide these agencies with new stimuli to continue to advance their expertise and strengthen their roles in setting global standards in their respective fields. Thus, the tripartite system ensured that agency expertise would continue to advance, and thereby remain relevant to the national development efforts supported by UNDP.

6. The tripartite system also included financial arrangements to reimburse agencies for the technical and administrative support costs associated with the execution of UNDP-funded projects. It was acknowledged from the outset that these costs should be shared between UNDP resources and the regular budgets of agencies. The original system reimbursed the executing agency 13 per cent of project expenditures, applied across-the-board to the totality of services provided, irrespective of the relative magnitudes of technical versus administrative support. Even though an executing agency might be involved to some extent over the entire life of a project (from formulation, design and appraisal, to implementation), reimbursement was made only on involvement at the project implementation stage, on the basis of project expenditures.

7. Over time, the system was said to have become volume driven, since reimbursement levels varied directly with the volume of project execution. Furthermore, the reimbursement mechanism did not facilitate the growth of national execution: although cooperating agency agreements permitted agencies to implement specific project components, there was no easy way for them to provide purely technical backstopping of nationally-executed projects. Nor was there a ready mechanism to reimburse agencies for their contributions at earlier stages of the project cycle (e.g., formulation and design) without also having them involved in implementation.

2. Evolving roles

8. The basic roles of the tripartite partnership began to come under pressure from shifts in the nature of development assistance over the last two decades, for example: fluctuations in overall ODA funding patterns; a push for greater programme focus; greater use of national capacities coupled with more targeted use of external expertise. UNDP's activities began to reflect more upstream, policy-oriented directions. This combined with the growth of national execution spawned changing roles in the tripartite partnership, which needed to be formalized and harmonized, through the establishment of more appropriate programming modalities.

9. In 1988 the UNDP Governing Council appointed an Expert Group to review the existing support costs system. This review coincided with major General Assembly reforms aimed at increasing the effectiveness and relevance of all United Nations operational activities. Thus, the reform of the support costs system should be seen in the context of the larger constellation of changing development priorities and interrelated United Nations system reforms, including the programme approach, national execution, and more effective country aid coordination.

10. What emerged in the main from this review was a call for a revised support costs system that would transform the basic roles of the tripartite partners. This revised system would enable Governments to assume the rightful role of ownership and execution of their development programmes, and to access upstream sectoral and policy advice, as well as technical implementation support for this purpose. UNDP would collaborate in the identification of programme approaches, the design of assistance and the mobilization of resources. Over time, agencies would increasingly focus on sectoral and policy advice and technical support to national execution, and gradually phase out direct involvement in the implementation and administration of projects. In addition, Governments would be able to select a cost-effective mix of implementation agents for procurement of project inputs, including national entities, NGOs and United Nations agencies, as appropriate.

3. Current support cost system ^{1/}

11. Thus, the successor arrangements for agency support costs established in Governing Council decision 91/32 were designed to achieve several key objectives through the introduction of the following features:

- (i) *Improve the technical focus of agencies, including their involvement in the "upstream" stages of the programme/project cycle; and reduce the administrative and operational involvement of the agencies in project implementation; through -*

^{1/} The current arrangements for agency support costs took effect on 1 January 1992, at the beginning of the fifth programming cycle, and became fully operational 1 July 1992. They were implemented under a set guidelines issued early in October 1992: Guidelines for the determination of execution and implementation arrangements, and Guidelines for the successor arrangements for agency support costs.

the clear separation of technical support services from administrative and operational support services with different reimbursement systems for each of the two sets of services.

- (ii) *Provide incentives for national execution, preserving the accountability of all parties, and ensuring that agency technical support services are available to the Governments, particularly for nationally-executed projects; through -*

a redefinition of the concept of execution (ownership and management of projects) and its separation from project implementation (procurement of inputs and their conversion to project outputs). This facilitated support to national execution, even as it became possible to engage a United Nations agency and/or other external agents to implement various project components.

- (iv) *Permit programme countries to exercise increased choice in programme implementation, through -*

the procurement of an optimal package of services from a varied range of implementing agents which includes NGOs, public institutions, national entities, as well as United Nations agencies.

12. The decision applied this new system only to the five large agencies 2/ which traditionally represented some 50 per cent of total project volume. The other smaller agencies continued under the "old regime", but were encouraged to join in the new system as soon as possible. The financial envelope for support costs was established at 14 per cent of the anticipated programmable resources for the fifth cycle with specific earmarkings 3/ made for the new facilities described below, as well as for the continuing arrangements for smaller agencies.

(a) Technical support services at the programme level - TSS-1

13. TSS-1 applies only to the five large agencies. Strictly speaking, it is not a reimbursement mechanism, but rather, a separate financial facility to permit agency participation in upstream policy and advisory areas. It can be used to procure agency technical services for sectoral policy advice and formulation of sectoral and cross-sectoral strategies and programmes. The Governing Council established a set of detailed procedures in decision 91/32 to identify the need for TSS-1 inputs, and appraise and approve requests. Agencies can decide to draw upon their own technical staff or use outside consultants, as necessary. This was intended to encourage agencies to refine and build-up their in-house technical expertise over time, in response to programme country demands.

2/ FAO, ILO, UNESCO, UNIDO and (then) UN/DTCD.

3/ The IPF-related portions of the original support costs envelope were reduced in line with the overall decline in actual programmable resources.

14. Reports over the cycle indicate that TSS-1 has been a successful element in the new system, and proven highly effective in engaging agencies in upstream activities, as intended. ^{4/} Proposals for TSS-1 support have far exceeded available funding, and in many instances have served as a catalyst to mobilize additional financial resources for upstream initiatives.

(b) Technical support services at the project level - TSS-2

15. TSS-2 is also applicable to the five large agencies and is a project level facility that permits access to technical support services from United Nations agencies irrespective of the implementation modalities. Whether a project is agency or nationally executed, TSS-2 budgets can be approved to ensure technical monitoring and backstopping from specialized agencies. TSS-2 can provide, for instance: technical advice and guidance to project staff; participation in project reviews; and advice to UNDP and Government on possible changes required during project implementation. Though primarily intended to provide technical support for implementation, TSS-2 can also be used for project formulation and appraisal. Agencies can provide these kinds of TSS-2 services without necessarily being involved in project implementation. Thus, the agencies can be used as technical partners, reinforcing the accountability of the Administrator, especially for national execution.

(c) IPF sub-line for administrative and operational services (AOS)

16. As part of the support cost arrangements introduced in the fifth cycle, recipient countries were assigned an additional 10 per cent of their IPFs as a sub-line. These funds can be used to reimburse implementing agents for the costs of providing administrative and operational services (AOS); that is, the costs associated with obtaining and administering the inputs required for development projects and programmes supported by UNDP. A common schedule of rates for six separate clusters of activities was established for the five large agencies, which works out to an average of 10 per cent of the value of the projects. ^{5/}

17. To obtain the various services required to implement a project or programme, Governments can access an optimal selection of implementing agents from a full range of possibilities which includes NGOs, public institutions, national entities, as well as United Nations agencies. These agents are reimbursed according to the applicable cluster rate. Any unutilized resources in the IPF sub-line can be used for additional programming, which serves as an

^{4/} The governing bodies of both UNESCO and FAO have formally expressed their appreciation of the TSS-1 facility in resolutions.

^{5/} These clusters and their percentage reimbursement rates are: international personnel (9%); national personnel (11%); sub-contracts (11%); fellowships (12%); other training services (21%); local procurement (6%); international procurement (10%) or (4%) for large purchase orders. Thus, an agency recruiting an international expert for a project, is reimbursed 9 per cent of the total costs of that expert to reflect the administrative costs of recruitment and personnel backstopping.

incentive for programme countries to undertake a substantial portion of implementation themselves, thereby building national capacities.

(d) Continuing arrangements for the smaller agencies

18. As noted in paragraph 12, the smaller technical agencies continued under the former support costs regime. Under this regime, they continue to be reimbursed support costs at a rate of 13 per cent of the project budgets they deliver as executing or cooperating agents. Where total project delivery for an agency falls below \$24 million annually, a supplementary flexibility payment is made to compensate for the diseconomies of scale associated with a low volume of project activities. ^{6/} The 13 per cent reimbursement is presently made from two sources. The 10 per cent for the AOS component is paid from the indicative planning figure (IPF) sub-line; the additional 3 per cent and flexibility, which together can be seen as the technical support element of support costs for smaller agencies, are paid out of centrally-held resources.

19. The sectoral support allocation of \$11 million for the fifth cycle enables smaller agencies without direct field representation to participate in activities such as programme formulation. ^{7/}

20. To help the smaller agencies undertake additional technical support activities in their respective areas of services, the Executive Board, in its decision 94/26, approved the redeployment of unutilized support cost resources to increase the original \$11 million sectoral support allocation for the smaller agencies to \$16 million.

(e) Overall Assessment

21. In compliance with decision 92/22, an external team of high-level consultants evaluated the current support cost arrangements in 1994 and reported to the Executive Board in document DP/1994/23/Add.1. The evaluators indicated that, at that time, there was insufficient experience to draw firm conclusions about the arrangements, but they did make several noteworthy observations and recommendations on operational and programmatic issues which continue to be taken up in ongoing consultations between UNDP and the agencies.

^{6/} This applies on a sliding scale based on the degree of shortfall under the \$24 million threshold, maximizing at an additional 9 per cent of total delivery.

^{7/} Although somewhat anomalous for a large agency, UNIDO continued to receive a separate \$19 million allocation under the sectoral support facility during the fifth cycle, for its country director programme.

22. It is normal to expect a period of transition from the long-standing previous arrangements where agencies had generally assumed an all-encompassing execution role. Under the new support cost arrangements, UNDP and Governments have modified their working modalities, as necessary, to make optimum use of agency technical expertise to support UNDP-financed programmes. Similarly, agencies have also devised ways to bring their support on board to respond effectively to the demands of national execution. The large agencies confirm that the trend is for them to focus on technical support and less on the administrative and operational side of projects.

4. Support costs under the successor programming arrangements

23. Assessment of operational experience with the current support costs system during the fifth cycle, inter alia, contributed to the simplified consolidation of the financial framework for support costs approved under decision 95/23 on the successor programming arrangements. Support costs are now encompassed under three financial lines, instead of the nine lines used in the fifth cycle. These are:

- (i) Line 1.6 - Support for implementation of programmes and projects: with an earmarking of 3 per cent of total core resources, this line finances administrative and operational services for country activities funded from TRAC lines, and intercountry activities funded from line 1.2 (regional) and part of line 1.3 (global and interregional). The provision assumes that at least 50 per cent of these activities will fall under the national implementation modality.
- (ii) Line 2.2 - United Nations system support for policy and programme development (SPPD): with an earmarking of 2 per cent of total core resources, this line incorporates current allocations for TSS-1 for the large agencies, the sectoral support provisions for smaller agencies, and a contribution to the UNIDO country director programme for 1997 only.
- (iii) Line 2.3 - United Nations system support for technical services at the project level (STS): with an earmarking of 1.6 per cent of total resources, this line finances technical services at the project level from all eligible specialized agencies and thus replaces both the TSS-2 facility for the large agencies, as well as the technical support component of the flat rate support cost reimbursements for the smaller agencies.

24. Under the successor programming arrangements, the current guidelines for support costs (see footnote 1) will continue to apply, mutatis mutandis, and will be modified only to the extent necessary to:

- (a) Accommodate the simplified system of support cost earmarkings outlined above;
- (b) Reflect experience with the support cost arrangements during the fifth cycle; and

(c) Ensure coherence with overall guidelines and procedures being established for the successor programming arrangements,

25. With reference to the latter point, it should be emphasized that the overall guidelines for the implementation of the successor programming arrangements will extend to support cost components, particularly the sections on the resource assignment process, the programme review, monitoring and oversight system, and the start-up and phasing-in procedures.

III. MODIFICATIONS TO THE SUPPORT COSTS SYSTEM

[Elaboration of proposed modifications to the operation of current support cost facilities, as set out in DP/1996/13]

[Advantages and disadvantages of possible alternative approaches to procurement of technical services] (*being developed*)