ADOPTION OF THE REPORT OF THE BUDGETARY AND FINANCE COMMITTEE
TO THE GOVERNING COUNCIL

Draft report of the Budgetary and Finance Committee

Rapporteur: Mr. K. Tenkorang (Ghana)

Addendum

CHAPTER IV. FINANCIAL, BUDGETARY AND ADMINISTRATIVE MATTERS

F. Agency support costs: statement by the Administrative Committee on Co-ordination on the effect of changes in the exchange rate of the United States dollar on support cost reimbursement by the United Nations Development Programme

1. For its consideration of item 9 (f) of the Council's agenda, the Committee had before it the note of the Administrator containing the statement of the Administrative Committee on Co-ordination (ACC) on the effect of changes on the exchange rate of the United States dollar on support-cost reimbursement by UNDP (DP/1988/66). ACC was requesting special ad hoc measures for support-cost reimbursement for 1987 as a result of the continued substantial depreciation of the United States dollar.

2. In introducing the item, the Deputy Assistant Administrator, BFA, stated that the request of ACC had the full support of UNDP. In a programme such as
that of UNDP, where income was received and programme expenditure incurred in a multitude of currencies, movement in exchange rates had direct repercussions on the financing of the programme. Since 1985, the weakening of the United States dollar against most European currencies had been dramatic. Whilst this movement had brought about a substantial increase in UNDP assets, it had had a totally negative impact on the financing of support in the European-based executing agencies. The Deputy Assistant Administrator stated that UNDP was well aware of the Council's concern regarding the level of UNDP resources applied towards programme and administrative support costs. However, the organizations in the United Nations system, particularly those based in Europe, were generally facing severe financial difficulties. The prime concern of UNDP was the quality of the programme which could be harmed by the effects of these financial difficulties.

3. The assistant-Secretary-General of the Office of General Services, United Nations, in his capacity as Chairman of the Consultative Committee on Administrative Questions (CCAQ), then introduced the ACC statement on behalf of ACC. He informed the Committee that, in addition to the member organizations of ACC, the request also had the support of the intergovernmental bodies of those agencies that had had the opportunity of reviewing it. He stated that to permit executing agencies to provide adequate technical and administrative support for efficient and effective programme delivery, it was necessary to have an infrastructure whose size could vary according to the demands of programme delivery. The infrastructure and the staff involved had to be administered and financed with reasonable predictability. He recalled that agencies had been making efforts, particularly in the recent past, to reduce the cost of the support infrastructure, as of their operations in general. Whilst these efforts would continue to be pursued, it was important that the purchasing power of the financial inputs for the support operations remain relatively stable. In that regard, he pointed out the drastic reductions in purchasing power in the headquarters locations of the European-based executing agencies caused by the sharp decline in the value of the United States dollar against the major European currencies.

4. To protect their regular budgets, agencies had introduced a variety of measures, such as split assessment schemes, advance purchases of foreign currencies, drawing on special reserve accounts or other funds, as well as
supplementary estimates. The representative of ACC recalled that the Governing Council, in decision 81/40 of 30 June 1981, had already recognized the principle of compensation for adverse currency fluctuations. ACC considered the proposal to be in line with that policy. It was larger in scope because the movement in exchange rates since 1985 and the scale of losses suffered were far greater than could have been foreseen at the time of the decision. The request for additional compensation related only to 1987 and would amount to some $3.5 million more than provided under decision 81/40. The representative of ACC further pointed out that the formula used to prepare the request recognized and took into account that some project expenditure had been incurred in currencies that had appreciated against the United States dollar and that not all support cost expenditure was made in the currencies of the headquarters locations. He emphasized that the request was to be considered as a special ad hoc measure for 1987 and was not intended to set a precedent for the period 1988 to 1991. He then referred to the period from 1981 to 1985, when the higher value of the United States dollar had brought benefits of higher purchasing power for executing agencies. He pointed out that these benefits had been more than offset by other factors, such as reduced programme delivery of UNDP-financed activities; inflation; the change in the programme structure towards short-term experts and national experts; Government execution; and the general financial position of agencies, which had decreased the flexibility with which they could deploy other funds to assist their support infrastructure. The ex post facto report clearly demonstrated that actual support-cost expenditures were substantially in excess of reimbursements received. The increased purchasing power during that period had served to relieve some of the burden placed on the regular budget resources to support programmes financed by UNDP.

Summary of the discussion in the Committee

5. Several members indicated that they supported the request of ACC. In doing so, they emphasized that the exception to decision 81/40 should not constitute a precedent. Two members stated that although they supported the request from a political standpoint, they were not wholly convinced by the arguments submitted. In addition, one member, recalling that the standard rate of 13 per cent was a compromise that assumed a sharing of the support cost, sought reassurance that approval of the request would not mean that
reimbursement to agencies exceeded actual costs of support. He further suggested that consideration be given to a formula for reimbursement based on a basket of currencies, thereby limiting the impact of currency fluctuations. Another member, noting the disparity on organizational and accounting structures evidenced by the ex post facto report, was not convinced of the correctness of the 20 per cent across-the-board adjustment made in the ACC calculations. Although she recognized the difficulties in calculating exact figures, she was concerned that the smaller agencies might be suffering more from the impact of the currency fluctuation. Another member recalled that the 13 per cent standard rate of reimbursement was known to be insufficient to cover the full costs of support. Moreover, decisions 80/44 of 27 June 1980 and 81/40 had assumed a steady growth in regular budgets of the agencies. However, the recent trend to zero-growth or reductions in regular budgets had affected their ability to subsidize the support costs. He recognized the need for additional compensation, noting that the amount requested was relatively minor compared to the gains from the appreciation of donors' contributions to UNDP. A further member expressed concern at the disturbing trend of increased subsidies from regular budgets. He was convinced by the arguments put forward by ACC and, noting the current financial strength of UNDP recommended prompt transfer of the funds requested. Another member, while supporting such a transfer, suggested that approval should be linked to certain requests for improvement in support that would be in the interests of all concerned.

6. A number of members, however, could not support the ACC request. Whilst they understood the difficulties faced by the agencies, they did not consider that the case had been sufficiently documented. In that respect, two members indicated that they could not agree with the across-the-board adjustment of 20 per cent in the calculations. Further, the members expressed concern that an exception to decisions 80/44 and 81/40 could become a precedent. They preferred to maintain the provisions of those two decisions. One member expressed disappointment that the agencies had not established cost measurement systems which would provide better data on which the Governing Council could deliberate. Another member sought clarification on the relative impacts of strong currencies at the agencies headquarters locations and the weaker currencies of the developing countries. He was also concerned at the prospect that further resources would be diverted from the developing countries.
7. Two members sought further clarification regarding the impact of the changes in the programme structure, particularly with regard to the cost of supporting national experts. One member, noting that regular budgets in many agencies had mechanisms to offset losses from currency fluctuations, inquired whether approval of the ACC request would in fact duplicate compensation. He suggested that agencies take steps to reorganize their support structures, which he considered to be too cumbersome. Another member asked for more information on the economies effected by agencies and the treatment of inflation in regular budgets. He also wished to know whether non-European-based agencies had suffered from adverse exchange rate fluctuations. One member, noting a substantial increase in the cost of international experts, asked whether the additional support costs arising from these inputs to projects offset the currency losses. He also wondered, in view of the continued strength of the European currencies, whether a similar request for additional support cost reimbursement would be made for 1988. Another member asked why the support-cost reimbursement rates for projects executed by the Office for Project Services (OPS) were lower than for other executing agencies.

Response of the Administrator and ACC

8. In respect of the question concerning the possibility of double compensation, the representative of ACC informed the Committee that the executing agencies generally had two kinds of activities: a regular programme financed through assessed contributions; and operational activities funded by voluntary contributions or by UNDP. The mechanisms to offset adverse currency fluctuations, to which he had referred in his introduction, related only to the regular programme. In the case of trust funds there was, in some cases, the possibility of renegotiating the project document. Regarding UNDP, the only recourse was to seek compensation from the Governing Council. There was no question of double compensation.

9. With regard to the question about the support requirements for national experts, the representative of ACC explained that the pattern of inputs to projects had shifted from long-term international experts. The trend was towards short-term experts or national experts, who also served for shorter periods. The cost of recruitment, travel, separation and other related backstopping was almost the same, whether an expert served a longer or shorter period. The increase in support costs was therefore more a reflection of the greater number of short-term assignments.
10. The representative of ACC further informed the Committee that several organizations were embarking on integrated computerized financial systems, which should, in time, lead to better information and cost reductions. Such systems, however, required a substantial capital outlay at the beginning. In the meantime, all agencies continued to take whatever smaller steps were possible to improve productivity.

11. With regard to accounting for inflation under regular budgets, the representative of ACC explained that governing bodies had taken different approaches, including supplementary estimates, withdrawals from reserves, working capital funds or other special accounts.

12. The representative of ACC further informed the Committee that only the European-based agencies had applied for the exceptional measures to compensate for the losses from currency fluctuations. In most of the other headquarters locations, the local currency had been relatively stable compared to the United States dollar.

13. In response to the general concern about approval of the ACC request becoming a precedent, the Deputy Assistant Administrator confirmed that the special measures related only to 1987 and that decision 81/40 would continue to apply in future. He further drew the attention of the Committee to the information contained in the *ex post facto* report, which clearly demonstrated that actual costs incurred exceeded the total reimbursements, including the ACC request.

14. With regard to the question concerning the increased costs of experts, the Deputy Assistant Administrator suggested that one should look at the total picture for delivery rather than single inputs. He assured the delegate that the losses sustained through currency fluctuations greatly exceeded the increased support-cost income from a higher project expenditure.

15. In reply to the question about rates of support-cost reimbursements for OPS-executed projects, the Deputy Assistant Administrator explained that OPS did not offer the full range of services normally provided by the specialized agencies. A large part of OPS-executed projects concerned procurement or were implemented through sub-contracts, usually to private consulting firms. As a result, the OPS overheads were lower.