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PROGRAMME BUDGET FOR THE BIENNIUM 1978-1979

Agency support costs

Twenty-second report of the Advisory Committee  
on Administrative and Budgetary Questions

1. The Advisory Committee on Administrative and Budgetary Questions has considered the report on agency support costs which the Administrator of the United Nations Development Programme prepared for the Intergovernmental Working Group on Support Costs of the UNDP Governing Council (DP/WGOC/25).
2. The Administrator states in the introduction that the report constitutes his response to a request addressed to him by the Working Group, at its second session in June 1978, for a modified formula for reimbursement of support costs in order to enable the Working Group to formulate an intergovernmental recommendation to the Governing Council. The Working Group specified in its decision that any new reimbursement formula should be easy to understand, practical and durable, and that, to the extent feasible, it should take account of several factors: economies of scale, nature and component mix of projects, method of execution, and also - but only if a simple way could be found - variations in cost levels at headquarters of executing agencies, a measure of stabilization in the year-to-year variations in reimbursements for support costs, and the calculation of support costs on a project basis. 1/
3. As requested by the Working Group, the Administrator held consultations with the executing agencies on such a modified formula. In paragraph 5 of his report, he states that in the course of those consultations he reiterated that it was imperative that the United Nations system collectively evolve a modified long-term arrangement with which the organizations could work and which would be generally acceptable to Governments. In paragraphs 6 and 7, he states that objections to and reservations on the formula that he was proposing have been made by the United

1/ Official Records of the Economic and Social Council, 1978, Supplement No. 13 (E/1978/53/Rev.1), annex III, para. 61.

Nations, the United Nations Industrial Development Organization and the Food and Agriculture Organization of the United Nations. In paragraph 8, he indicates that all the other executing agencies have indicated that they would accept his proposals.

4. The United Nations Development Programme currently plays to the executing agencies support costs amounting to 14 per cent of programme delivery, with flexibility arrangements for agencies delivering a programme of less than \$10 million a year. The Administrator recommends that this uniform rate be replaced by variable rates. In paragraph 46 of his report, he summarizes the main points of his proposal as follows:

A. Flexibility arrangements

Agencies with annual programme delivery levels below \$15 million would be reimbursed in excess of 14 per cent upon presentation of detailed cost information justifying the increased reimbursement. The Administrator would authorize the amount of reimbursement and would inform the Governing Council of this action. Cases of special hardship arising from significant currency fluctuations and not already covered by the foregoing flexibility provisions would be referred, on an ad hoc basis, to the Governing Council.

B. Economies of scale

Agencies with annual programme delivery levels between \$15 and \$50 million would receive, subject to C below, reimbursement at the rate of 14 per cent of programme delivery. For the \$25 million portion between \$50 and \$75 million delivered, the reimbursement rate would be 13.5 per cent; between \$75 and \$100 million, the reimbursement would be at the rate of 13 per cent; and the amount over \$100 million would be reimbursed at 12 per cent.

C. Nature and component mix of projects

For projects consisting of 75 per cent or more of equipment and/or subcontract components, the reimbursement rate would be 7 per cent of total project costs. The totality of these projects would be excluded on an agency-by-agency basis before reductions were made with respect to economies of scale.

D. Special arrangements with the International Bank for Reconstruction and Development and UNDP/OPE

The present special arrangement providing for a consolidated, reduced rate of 11 per cent reimbursement would continue in respect of IBRD. The present arrangements for approval by the Governing Council of the annual

budget estimates in respect of support services for UNDP/OPE projects would also be continued.

E. Method of execution

In the case of government execution, agencies would be reimbursed 14 per cent of the amount of the project elements that they were asked to execute on behalf of the Government, unless the services were provided for the procurement of equipment, in which case the reimbursement rate would be 7 per cent.

F. Date of application

The modified formula would take effect as from January 1982 and would remain in force for the succeeding two IPF cycles, i.e. until 1991. In 1989, the situation would be reviewed and a decision would be taken with respect to the period beyond 1991.

5. Inasmuch as the proposed formula will lead to smaller payments to the agencies executing larger programmes, the Administrator has made provision for transitional arrangements. The objective is that for every agency the dollar amount of reimbursement in 1981 under the current 14 per cent formula would be safeguarded, provided that the annual total of project expenditures for that agency continued to remain at or above the 1981 level, until such time as the application of the modified formula produced the 1981 amount of reimbursement (DP/WGOC/25, para. 7 and annex, para. 6).

Observations of the Advisory Committee

6. In considering the Administrator's recommendations, the Advisory Committee recalled that while there is no unanimity among Member States concerning the role which the assessed budgets of the agencies should play in the technical assistance activities of the United Nations system, the basic principle that has been consistently applied since the emergence of technical assistance activities is that the organizations provide a portion of the support costs of the extrabudgetary programmes from within their regular budgets. This principle recognizes that the relationship between the executing agencies and the funding agencies is one of partnership. 2/

7. The executing agencies reported to the Advisory Committee that in 1977 their assessed budgets contributed \$37.3 million towards the support costs of projects financed from extrabudgetary funds, and that the corresponding estimates for 1978 and 1979 are \$41.7 million and \$43 million respectively (A/33/309, para. 24, table C). Admittedly, in the absence of general agreement on what should be

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2/ This aspect of the question was last discussed by the Advisory Committee in its report to the Governing Council of UNDP in June 1977 under the symbol DP/284. See Official Records of the General Assembly, Thirty-second Session, Supplement No. 8A (A/32/8/Add.1-30), document A/32/8/Add.9, annex.

included in support costs and of procedures for measuring what is deemed to form part of those costs, the given totals can only be regarded as approximations. None the less, it remains a fact that the assessed budgets of the executing agencies contribute a substantial proportion of the support costs of operational programmes financed from extrabudgetary funds.

8. Inasmuch as the administrative costs incurred by UNDP itself also form part of the support costs of technical co-operation, these support costs include three elements: (a) the administrative budget of UNDP, (b) the UNDP reimbursement to the executing agencies, and (c) the contributions by the regular budgets of the specialized agencies. As the Advisory Committee has repeatedly pointed out, most recently in its report to the Governing Council of UNDP in June 1977, a natural corollary of the foregoing is that both the funding and the executing organizations should be interested in improving effectiveness and economy in the delivery of projects. 3/

9. The Advisory Committee notes that the proposals by the Administrator do not address themselves to the ways and means of reducing the totality of support costs. They can be regarded as dealing with a redistribution of those costs between UNDP and the executing agencies.

10. Of the several proposals put forward by the Administrator (see para. 4 above) the one that would have the greatest impact, if accepted, is the introduction of a regressive rate of reimbursement for programmes in excess of \$50 million in annual deliveries, on the grounds of "economies of scale".

11. The Advisory Committee recalls that, in its report to the Governing Council in June 1977, it recommended that the Administrator and the executing agencies study the possible introduction of variable rates and report their conclusions to the Governing Council. 4/

12. In paragraph 32 of his report in document DP/WGOC/25, the Administrator states that an analysis of the data for the three-year period 1975-1977 did not reveal a clear-cut pattern and that it was difficult to measure changes in the relationship between the level of delivery and support costs. The difficulties were due to several factors, including, in particular, currency fluctuations and inflation. In paragraph 35, the Administrator says that a pragmatic approach must be used to establish the plateaux beyond which reduced reimbursements may be contemplated. His proposals, based on such a pragmatic approach, are set out in paragraphs 35 and 36 of his report (see para. 4B above).

13. Furthermore, the Administrator's proposals do not provide for the gradual adjustment of the thresholds to take care of inflation. If, as the Administrator suggests, the dollar amount of the thresholds is to remain unchanged for 10 years (from 1982 to 1991), inflation at an annual rate of 7 per cent would reduce the

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3/ Ibid., annex, para. 9.

4/ Ibid., annex, para. 11.

purchasing power of \$100 million to about \$50 million and of \$50 million to about \$25 million. In other words, the reduced 13.5 per cent reimbursement rate would be applied beginning with a level of programme delivery that would be only \$10 million (in 1982 dollars) more than the limit for the application of flexibility provisions for smaller programmes; and a rate of 12 per cent would come into operation at a level (in 1982 dollars) at which reimbursement would be made at 13.5 per cent in 1982.

14. In the opinion of the Advisory Committee, the objective of a regressive formula reflecting economies of scale should be that the assessed budgets of the agencies should not profit from the execution of UNDP-financed projects by receiving more by way of reimbursement than they spend on support costs. So long as an agency's expenditure on support costs exceeds the amount of reimbursement, any decrease in the rate for the latter will increase the amount chargeable to the assessed budget.

15. The Advisory Committee has no objection in principle to the concept of a lower rate of reimbursement depending on the nature and component mix of projects and the method of execution (see para. 4C and E above).

16. At present levels of programme delivery, there is need for the regular budgets of the executing agencies to contribute to project support costs. The amount of this contribution has been increasing (see para. 7 above) and it is likely that this trend will continue with the growth of the volume of UNDP-financed projects executed by the agencies. Admittedly, a stage may be reached when the economies of scale will begin to have a significant effect. But the gap between the current level of agency support costs and the 14 per cent rate of reimbursement now seems to be such that the threshold at which the rate of reimbursement may be reduced will have to be considerably higher than has been proposed by the Administrator. Alternatively, if the standard rate of reimbursement were set at 15 or 16 per cent, the threshold at which the reduced rate would operate could be set lower than if the 14 per cent rate were retained, without imposing an additional burden on the regular budgets of the agencies. Furthermore, periodic adjustment of all thresholds would be needed to counter the effects of inflation and currency instability.

17. The Advisory Committee appreciates the efforts made by the Administrator to work out a formula that would be generally acceptable. The Committee is not convinced, however, that the proposals in document DP/WGOC/25 can be regarded as meeting the criterion of general acceptability. Furthermore, the Committee points out that it has not been proved that the proposals have significant advantages, on technical grounds, over the present approach of applying a uniform reimbursement formula. Should Member States nevertheless decide, on political grounds, that the Administrator's proposals be accepted, the Advisory Committee would recommend that they be adjusted to take full account of the Committee's observations in this report.

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