GOVERNING COUNCIL
INTERGOVERNMENTAL WORKING GROUP ON OVERHEAD COSTS
First session
January 1978

DRAFT REPORT OF THE INTERGOVERNMENTAL WORKING GROUP ON OVERHEAD COSTS

(Part I (draft) of the Working Group's interim report to the Governing Council at its twenty-fifth session)\(^1\)/

Rapporteur: Mr. Peter OSVALD (Sweden)

INTRODUCTION

1. The intergovernmental Working Group on Overhead Costs, which was established by the Governing Council of the United Nations Development Programme at its twenty-fourth session (E/6013/Rev.1, para. 348), held its first session at United Nations Headquarters on 16-17 January 1978.

I. ORGANIZATION OF THE SESSION

Attendance

2. Members of the Governing Council represented at the session of the Working Group, States represented by observers, and organizations in the United Nations system and other intergovernmental bodies are listed in the annex to the present report.

\(^1\)/ The Working Group agreed at its first session that this draft would be considered and approved at its second session, in June 1978.

78-02467
Election of officers

3. The session was opened by the President of the Governing Council who referred briefly to the terms of reference of the Working Group and the decision of the Governing Council establishing it, and pointed out that it was open to all members of the Council, as well as to observers from other Member States. The President proposed that the Group choose its own Chairman and suggested that Mr. Sarfraz Khan MALIK (Pakistan), the First Vice-President of the Council, who was also the Chairman of the Budgetary and Finance Committee, be elected. The Group agreed to this suggestion and elected Mr. Malik Chairman.

4. In his opening statement the Chairman suggested that the Working Group elect a Rapporteur and suggested that since a representative of Sweden was the Rapporteur of the Budgetary and Finance Committee, the same arrangement be made for Rapporteur of the Working Group as well. This suggestion was accepted and Mr. Peter OSVALD (Sweden) was chosen Rapporteur.

Agenda and organization of work

5. The Chairman welcomed the Administrator of UNDP and his associates as well as the representatives of the Executive Heads of several Agencies and invited them to participate actively in the work of the Group.

6. The Chairman then drew attention to the provisional annotated agenda (DP/WGOC/16) which he considered reflected the general expectation that the first session of the Group would be an organizing and preparatory session devoted to determining (a) how the Group wished to approach its task and try to identify the various elements or questions to be examined; (b) a review of the documentation available and comments on them as well as any expression of general views; (c) the identification of the further information and documentation which the Group may need for its further work from the Administrator, Heads of Agencies or other entities; and (d) the programme and time-table for future work. He then referred to the documentation that had been provided which contained the views of the Executing Agencies, the Advisory Committee on Administrative and Budgetary Questions (ACABQ), the Board of Auditors, the Joint Inspection Unit (JIU). The Chairman also suggested that an interim report to be submitted to the Governing...
Council in June 1978 might incorporate the results from the present session as well as the second session planned for early June and might be approved in June. It was agreed that this was an acceptable method of proceeding and document DP/WGOC/16 was accepted as a guide for proceeding with the work of the first session.

7. In addition to the annotated agenda (DP/WGOC/16), the Working Group had before it the following documents:
   (a) Two Notes by the Administrator (DP/WGOC/11 and DP/WGOC/CRP.1 and Corr.1)
   (b) Views of the Advisory Committee on Administrative and Budgetary Questions (DP/WGOC/10)
   (c) Views of the United Nations Audit Operations Committee (DP/WGOC/8)
   (d) Views of the Joint Inspection Unit (DP/WGOC/1)
   (e) Views of the Specialized and Executing Agencies: ICAO (DP/WGOC/2); WHO (DP/WGOC/3); UNIDO (DP/WGOC/4); FAO (DP/WGOC/5); WMO (DP/WGOC/6); World Bank (DP/WGOC/7); ILO (DP/WGOC/9); ITU (DP/WGOC/12); UNESCO (DP/WGOC/13); WIPO (DP/WGOC/14); UPU (DP/WGOC/15); United Nations (DP/WGOC/17).

II. INTRODUCTORY REMARKS BY THE ADMINISTRATOR

8. In his opening remarks to the Working Group, the Administrator referred to the very complex nature of the overheads question and to his view, which he had stated at the twenty-fourth session of the Council in June 1977, that the question had much broader dimensions than purely financial ones and that it had to be resolved through a policy decision by Governments through mutual consultations and consensus in the appropriate intergovernmental bodies. It was for this reason that he had submitted a paper to the twenty-fourth session (DP/259) outlining several options rather than a specific recommendation for consideration by Governments. The Administrator had not departed from that position and, for that reason, had not submitted a position paper at this stage. A resume of the background to the problem over the years had nevertheless been provided (DP/WGOC/CRP.1). The Administrator also underlined that the introduction of any new arrangements
must be according to a mutually agreed time schedule, taking into account the normal budgetary processes and cycles of the several organizations; this is a point to which he and the Executive Heads of the organizations attached special importance. He added that in the light of the expected time-table of the Working Group and of the budgetary cycles of the organizations, it was reasonable to suggest that any new arrangements could not be implemented earlier than 1982, which also would coincide with the start of the next IPF cycle.

III. SUMMARY OF DISCUSSION

9. In view of the interrelatedness of the agenda items, most members referred to them interchangeably. The following summary, therefore, does not relate to any item exclusively nor is it arranged in chronological fashion; it highlights the significant points made in the discussions that took place.

10. During the discussion several members as well as the Chairman stressed the importance of considering three basic points that needed to be addressed by the Working Group (a) determination of the proper terminology to be used, the term "support costs" being favoured by most speakers, as well as its clear definition including a listing of the cost elements to be covered under the definition; (b) a system or the means for calculation of these cost elements; and (c) an arrangement for the distribution of these costs between UNDP and the Agencies. It was generally agreed that point (c) was a matter for an intergovernmental policy decision and would arise at a somewhat later stage in the review of the question of overheads.

11. Several members referred to the criteria to which any new system should conform and which had been outlined in the Governing Council decision of June 1977. They felt that it was essential to seek reductions in the costs associated with the delivery of technical co-operation programmes in order to make the maximum resources available for direct assistance to the developing countries. In this connexion, it was pointed out that over the period 1972-1976 UNDP and Agency overheads had increased more rapidly than project costs. Several members felt that the system should have a built-in incentive element to achieve this purpose. One member thought that the new system should have an internal control mechanism to ensure
that maximum utility was obtained from the funds provided for "overhead" support functions which would also act as an incentive to reduce such costs. The new system should be simple and should be applicable to all extrabudgetary technical co-operation activities of the United Nations system. Several members referred to the principle of partnership in sharing the costs of the functions between UNDP and the Agencies as well as taking into consideration the special situation of the smaller Agencies. It was pointed out in this regard that support for technical co-operation activities had increasingly become an important function of the Agencies. One member felt that it was important for the developing countries to be able to participate in determining the amount of overhead to be paid. The point was also made that an account should be available, preferably to the Governing Council of UNDP, of how Agencies utilized overhead reimbursement moneys.

12. Agency representatives stressed the importance of stability in knowing how much they could expect to receive in the form of overhead reimbursement in order to plan their activities and support functions accordingly. While one Agency opted for full reimbursement of overhead costs, Agencies on the whole favoured the acceptance of the present 14 per cent compromise arrangement as a permanent solution. They doubted whether a continued effort could bring about a new long-term solution. However, most Agency representatives declared that they were prepared to participate in the discussion and elaboration of any alternative system.

13. Most speakers referred to the JIU proposal contained in document DP/WGOC/1. Although a few members expressed disappointment at this proposal, it was generally agreed that the proposal could serve as the starting point for further discussion if it were elaborated with greater detail. It was specifically suggested that the JIU be requested to expand and complete its Note, including the percentages and special formulae in the table at the end of the Note, for consideration by the Working Group at its next session. It was further suggested that UNDP and the Agencies should submit their separate views on the JIU proposal contained in DP/WGOC/1 as soon as possible and also on the new and expanded JIU Note when that was available.
14. It was also pointed out that the breakdown into the component elements of the support function reflected in the JIU proposal would help in a better understanding of that function and would facilitate dealing with situations where only some, and not all, of the support elements might be involved.

15. At the same time, it was pointed out that the JIU proposal did not contain the incentive required to reduce over-all costs. One member cautioned that if different rates were applied to different Agencies, or on the basis of the different mix of component parts, distortions might develop in the decision-making process of Governments concerning the best method for project execution. Another member thought it particularly important to focus on differences emanating from the different mix of project components; the present practice of paying 14 per cent with respect also to equipment purchases appeared, to his Government, as a commission to the Agencies. It was suggested that in the further elaboration of the JIU proposal greater attention should be paid to Government execution and its consequences for overheads. Although several members were favourable to the approach of allowing for differing costs at the headquarters locations of the Agencies, one member stated that his Government had expressed its opinion on the subject of inflation and high cost-of-living during the General Assembly and that a solution to this problem should be sought in a wider context.

16. The need to look at the impact of any new system in monetary terms was emphasized. Some reservations were expressed on the JIU suggestion that, for ensuring a measure of stability, UNDP reimbursement of support costs should not, as a rule, decline by more than 10 per cent from one year to the next. One member, however, welcomed the principle behind this suggestion.

17. One member cautioned against the elaboration of too "scientific" a system, and advocated a more pragmatic "political" approach. Another member stated that a further elaboration of the JIU proposal should not be regarded as a package to be accepted or rejected in total by the Working Group.

18. The Working Group had an opportunity to hear Inspector Bertrand of the Joint Inspection Unit who provided some clarification of the JIU Note. He pointed out at the outset that the problem was twofold - technical, i.e., defining what was meant by the term and calculating the costs of the elements included and political, i.e., determining how the costs should be apportioned between the organizations.

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He reiterated that the present arrangement was a compromise reached with great difficulty. The Cost Measurement Study (CMS) showed that the Agencies were not sufficiently equipped from the technical point of view to carry out the study effectively. At the time the JIU stressed the need to modernize the accounting systems within the Agencies but only FAO had done so. He felt that the situation today is different because of the new orientation being given to technical co-operation activities as defined in Governing Council and General Assembly decisions. He cautioned that the JIU Note in document DP/WGOC/1 was preliminary at this time. He hoped that if the Group wished the JIU to elaborate the proposal, concrete instructions would be given. He also drew the attention of the members to the JIU Study on the Role of Experts, the draft report on which had just been sent to the Agencies for comment. He believed that the outcome of that Study would have considerable impact on the question of overheads. In response to a question, Inspector Bertrand added that the percentages and other details in the table at the end of the JIU Note would be filled in on the basis of information derived from CMS as well as any new elements obtained from the Agencies.

With regard to the JIU Note, several Agency representatives expressed regret at not being in a position to comment officially on the proposal since they had only just received it. However, the first reactions were generally favourable to the suggestion of using the proposal as a starting point for further elaboration and discussion. One Agency representative pointed out that it might be costly to implement but that if it eventually resulted in lower over-all costs, it might be worth the effort. Another Agency representative was pleased to see that it contained a provision for special arrangements in respect of Agencies with their headquarters in high dollar cost locations. Yet another Agency representative saw merit in relating the JIU proposal to the Study on the Role of Experts. The representative of one Agency underlined that a possible cost element system had been studied by his Agency on an earlier occasion and found to be too cumbersome and too costly. The JIU proposal might also have grave consequences on the concept of partnership between UNDP and the Agencies. He also felt that the proposed system might lead to project-by-project negotiation of overhead reimbursement.

Several members underlined in this regard the importance of receiving the Study on the Role of Experts in sufficient time for the Working Group, at its June 1978 session, to consider its relationship to the overhead question.
The Assistant Administrator, Bureau for Administration, informed the Working Group that the final version of the Study would be available to Governments in April. The JIU Inspector provided further information regarding the nature of the Study. He explained that the Study followed the line given by the Governing Council and endeavoured to set out a modular system for carrying out projects, leaving the Governments free to choose from a variety of methods for implementing projects. The practical consequences of this approach, in terms of support costs, still would have to be worked out since the role of UNDP and the Agencies in these new modalities might differ from the present. The Chairman confirmed that the Working Group at its next session should have available to it the JIU report on the Role of Experts so that the Group could take account of the conclusions of that report and their impact on the overheads question.

21. Several members referred to other options, in addition to the JIU proposal, that were available for discussion. Attention was invited to the options contained in the Administrator's report (DP/259) which had been submitted to the Governing Council at its twenty-fourth session. One member stressed that the solution to the question of overheads lay in a system combining several of those options. The important point was that the recipient Governments should be more involved in the execution of projects and equally in the determination of the amounts of overhead to be reimbursed. It was suggested that recipient Governments should have greater flexibility in negotiation both in regard to methods of execution and as to their cost. The automatic application of any single standard arrangement to all cases, regardless of nature, size and mix of projects, would not be logical, and Governments should have a greater say, especially in the case of large projects. This would be facilitated, it was suggested, by the inclusion of overheads in individual project budgets. Another member suggested a combination of a percentage of all project costs to cover fixed costs and a reimbursement of other supplementary costs. Yet another member pointed out the need to concentrate discussion on the cost of hiring experts.

22. Some members expressed the view that, given that technical co-operation had become an important, and even integral, function of the organizations, all overheads should be included in their regular budgets. One member holding this view suggested that better control by Governments and, therefore, greater efficiency and economy would be facilitated by putting all support costs in the regular budget. However,
reservations were expressed to any inclusion of overheads in regular budgets by some members, who based their objection on the voluntary nature of contributions for technical assistance activities.

23. Considerable discussion was devoted to past studies. Several members felt that past studies on the issue were useful but that they had failed to bring about a long-term solution. It was suggested that past studies need not be ignored and that they could provide valuable information on which to base a further study of the matter, such as the proposed elaboration of the JIU Note. One member found the 14 per cent formula satisfactory because his delegation felt that the pragmatic reasons and essential bases on which it had been decided had not changed significantly. However, many members felt that the situation had changed considerably and that the present formula was no longer suitable. The representative of the United Nations explained that the United Nations had come to the position of supporting the 14 percent as the most viable solution after many years of study together with the Agencies, the Administrative Committee on Co-ordination and internal working groups, because it was the most technically practical. The Secretary-General's position on the matter is given in documents A/C.5/31/33 and A/C.5/32/29. He asked for clarification of why members thought past studies had not produced workable solutions and why the present arrangements were considered out-of-date and deficient. In answer to this inquiry, the Chairman explained that the Governing Council was aware of the past history of studies and discussions on the issue and yet it had decided to set up the Working Group. The Cost Measurement Study, which formed part of the past history, was submitted to the nineteenth session of the Council but was not considered as having solved the question. He pointed out that the 14 per cent solution was a temporary compromise and an interim solution agreed upon only until such time as a better measure and formula could be developed and adopted. There seemed to be agreement that the present formula did not take into account different situations such as the location of an Agency's headquarters or the nature of the projects or the differing arrangements in the Agencies for handling these activities. Governments did not have available to them adequate information on how overhead payments were being utilized. The Agencies had reported to the Advisory Committee on Administrative and Budgetary Questions that their annual support costs for technical assistance activities were in excess of reimbursements by $40 million, but no breakdown had been provided to explain this figure nor was
it possible to determine how much of this amount would have been saved in the regular budget had there been no extrabudgetary technical assistance activities. One member went on to explain that if a majority of Governments had felt that the 14 per cent figure were a valid long-term solution, the Working Group would not have been set up. Another pointed out that the amount of past work, however voluminous, meant little if it did not produce the desired results.

24. The representative of UNIDO, who had been the Chairman of the CCAQ Task Force on the Cost Measurement System in 1974, provided some background on the CMS study. He pointed out the difficulties in making the information comparable among the Agencies; the Task Force had divided the component support elements into more than 100 subgroups in order to study them more carefully. The Task Force recognized that there were differences between Agencies, due in part to the level of costs incurred in the headquarters cities and, in part, to variations in the size and length of projects. He felt that sufficient data were already available and there was no need to carry out further studies. Responding to this line of argument, one member cited his Government's reservations regarding the CMS study. To begin with, he said, the cost elements which were included had not been agreed to by Governments; many elements were not clearly identified additional costs; the study was only carried out in five Agencies and therefore could not be generalized to cover all; even those five Agencies showed such wide variations as to invalidate the use of a single, flat average; and the study was carried out only for one year, 1973, which was a year of low delivery and the results could not validly be extrapolated. For these reasons, his Government did not think the results were conclusive enough to set a new formula. Another member pointed out that any new formula might perhaps be more complex, because it might be more exact, but if it achieved the objectives of greater efficiency and lower cost, the effort involved would be justified.

25. In regard to the basic points to be addressed by the Working Group (see para. 10 above), the discussion reflected the following trends. As regards terminology and definition, there was wide agreement, first, on the term "support costs" as more meaningful and, second, on the criteria for the definition of support costs outlined in paragraphs 7-11 of the JIU Note. One member felt that the definition contained in document DP/WGOC/6 was preferable, while another member thought that a change of terminology would not change the content of the term.
26. With respect to the means for calculation of the agreed cost elements, it was generally felt that, in addition to the elaboration of the preliminary JIU Note, the Group should have information on the various points and questions that had been raised in the discussion. Several Agency representatives provided preliminary data to be elaborated in the written submissions of their Executive Heads which were requested in the decision of the Working Group.

27. The Chairman summarized the points of agreement that had been reached and the list of matters on which further information was required. The Working Group agreed with the Chairman's summation and adopted the decisions outlined by him. The Chairman subsequently circulated a Note containing the consolidated text of these decisions (DP/WGOC/18).

28. In closing the first session of the Working Group, the Chairman stated that the first session, in his view, had been decidedly fruitful; it had not been an exercise in futility, as one participant had suggested, but one of utility. The Chairman also indicated, and the Working Group agree, that the next session would be held beginning on 5 June 1978, that is, during the week preceding the June session of the Governing Council. He requested the Agencies to submit their views on the JIU proposal contained in document DP/WGOC/1 as soon as possible so that the JIU could take these views into account when preparing its expanded Note. In connexion with the documentation to be made available for the next session, it was indicated to the Working Group that while every endeavour would be made to submit the documentation as expeditiously as possible, some flexibility in regard to the six-week rule might be needed.

Decision of the Working Group

29. As indicated in paragraph 27 above, the decisions adopted by the Working Group on 17 January 1978 on the basis of the Chairman's summation are incorporated in the consolidated text, which is reproduced below:

The intergovernmental Working Group on Overhead Costs

Having noted with appreciation the documents submitted to it at its first session in January 1978,

1. Broadly endorses the criteria for the definition of overheads (support costs) outlined by the Joint Inspection Unit (JIU) in paragraphs 7-11 of its Note (DP/WGOC/1);
2. Requests the Administrator of UNDP and the Executive Heads of the Agencies, through the Administrator, to make available to the JIU and to the Working Group their further comments on the JIU Note contained in document DP/WGOC/1;

3. Requests the Executive Heads of the Agencies to submit to the Working Group the following additional information:
   (a) A statement from each Agency briefly describing the organizational and other arrangements in the Agency to provide support to (i) UNDP-financed programmes and projects and (ii) other technical co-operation programmes and projects;
   (b) A statement from each Agency on the measures taken in the Agency to reduce support costs;
   (c) A statement from each Agency on the measures taken to decentralize responsibility and authority to the regional and country level and indicating the impact of those measures on support functions and costs;
   (d) A statement from each Agency briefly describing (i) the budgetary treatment of overhead payments received from UNDP and from other extrabudgetary sources, and (ii) the arrangements for, and extent of, intergovernmental review of the utilization of such overhead payments;
   (e) A statement from each Agency, where applicable, showing to what extent, how and where its regular budget provides for subsidies towards meeting attributed overhead costs;

4. Requests the Administrator to submit the following additional information:
   (a) A breakdown of numbers of projects by Executing Agency and size of project (size of UNDP allocation, in four or five size categories) for the years 1972-1976;
   (b) A breakdown of project costs by Executing Agency and component for the years 1972-1976;

5. Requests the JIU to submit a further and expanded preliminary note elaborating its outline of a new system for support costs as contained in DP/WGOC/1, including the completion of the percentage figures and the special formulae to be incorporated in the table at the end of that document, taking account also of economies of scale and nature (including size) of projects; the note should also explain the factors which account for variations in average overhead costs in different Agencies, including the impact of exchange rates and cost-of-living factors; requests the Administrator and the Executive Heads of the Agencies to submit to the Working Group their comments on this JIU Note;
6. Further requests the JIU to make available to Governments, members of the Working Group, copies of its forthcoming report on "The Role of Experts in Development Co-operation" as soon as it is issued; requests the Administrator and the Executive Heads of the Agencies to make available to the Working Group their comments on the above-mentioned report which they will be submitting to the Governing Council;

7. Requests the Advisory Committee on Administrative and Budgetary Questions to submit any further comments it may have on the general question and also on the proposals contained in the expanded preliminary Note of the JIU mentioned in paragraph 5 above;

8. Looks forward to receiving the information requested in the foregoing paragraphs in time for consideration at the Working Group's next session beginning on 5 June 1978.
ANNEX

REPRESENTATION AT THE FIRST SESSION OF THE
INTERGOVERNMENTAL WORKING GROUP ON OVERHEAD COSTS a/  

Members of the Governing Council

Argentina, Australia, Austria, Belgium, Brazil, Burundi, Canada, Colombia, Cuba, Czechoslovakia, Democratic Yemen, Denmark, Ecuador, Finland, France, Federal Republic of Germany, Guinea, India, Indonesia, Iran, Italy, Ivory Coast, Japan, Jordan, Kenya, Kuwait, Madagascar, Mali, Mexico, Netherlands, Norway, Pakistan, Poland, Romania, Senegal, Sierra Leone, Spain, Swaziland, Sweden, Switzerland, Thailand, Trinidad and Tobago, Tunisia, Union of Soviet Socialist Republics, United Kingdom of Great Britain and Northern Ireland, United States of America, Yemen.

States represented by observers

Barbados, Bangladesh, Bolivia, Cape Verde, Chad, Chile, China, Egypt, Gabon, German Democratic Republic, Greece, Guatemala, Honduras, Hungary, Israel, Jamaica, Lao People's Democratic Republic, Malta, Mauritania, Mongolia, Nepal, Niger, Portugal, Republic of Korea, Rwanda, Sri Lanka, Sudan, Surinam, Viet Nam, Togo, Turkey, Uruguay, Yugoslavia.

United Nations and related bodies


Specialized Agencies


Other intergovernmental organizations

Inter-American Development Bank, Organization of American States, World Tourism Organization.

a/ States and Organizations which communicated the names of their representation for the January 1978 meetings of the Governing Council and/or the Intergovernmental Working Group.