

برنامج
الأغذية
العالمي



Programme
Alimentaire
Mondial

World
Food
Programme

Programa
Mundial
de Alimentos

**Executive Board
Second Regular Session**

Rome, 8–11 November 2010

RESOURCE, FINANCIAL AND BUDGETARY MATTERS

Agenda item 5

For approval

E

Distribution: GENERAL
WFP/EB.2/2010/5-A/1
7 October 2010
ORIGINAL: ENGLISH

FINANCIAL FRAMEWORK REVIEW



This document is printed in a limited number of copies. Executive Board documents are available on WFP's Website (<http://www.wfp.org/eb>).

NOTE TO THE EXECUTIVE BOARD

This document is submitted to the Executive Board for approval

The Secretariat invites members of the Board who may have questions of a technical nature with regard to this document to contact the WFP staff focal points indicated below, preferably well in advance of the Board's meeting.

Deputy Executive Director and Chief Financial Officer, RM*:	Ms G. Casar	tel.: 066513-2885
--	-------------	-------------------

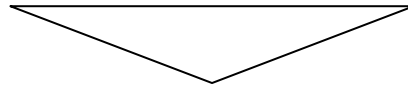
Deputy Chief Financial Officer and Director, RMB**:	Mr S. O'Brien	tel.: 066513-2682
--	---------------	-------------------

Should you have any questions regarding matters of dispatch of documentation for the Executive Board, please contact Ms I. Carpitella, Administrative Assistant, Conference Servicing Unit (tel.: 066513-2645).

* Resource management and accountability department

** Budget and programming division

DRAFT DECISION*



The Board approves the changes to General Rule XIII.4 and Financial Regulation 1.1 as set out in the document Financial Framework Review (WFP/EB.2/2010/5-A/1).

* This is a draft decision. For the final decision adopted by the Board, please refer to the Decisions and Recommendations document issued at the end of the session.

BACKGROUND

1. The financial framework review was undertaken to ensure that WFP's financial framework fully supports the implementation of the WFP Strategic Plan (2008–2013). A broad range of issues has been discussed in the context of the review, including:
 - programme categories;
 - the tonnage-based budgeting and costing model; and
 - funding of direct and indirect support costs.
2. Two related issues – advance financing/forward purchase mechanisms and prioritization – also emerged during discussions on the financial framework review.
3. Over the course of several informal consultations and Board sessions, the Secretariat received guidance from members on how to proceed in conducting the review. In the early stages, members prioritized issues related to programme categories, and these were subsequently split from the more financial issues at the 2010 Annual Session of the Board. Proposals for changes to WFP's advance financing/forward purchase mechanisms are also being addressed separately and will be presented at the 2010 Second Session of the Board. Prioritization issues have been discussed at several informal consultations and remain an important feature of the ongoing dialogue with the Board on resource management issues.
4. Discussions of issues related to the tonnage-based model and the funding of direct and indirect support costs have continued in parallel with these efforts. At the Board's 2010 Annual Session, the Secretariat presented "Financial Framework Review Options" (WFP/EB.A/2010/6-E/1) outlining six recommendations:
5. **Recommendation 1.** Segregate non-commodity activities within projects and – exceptionally – allow separate funding streams.
6. **Recommendation 2.** Modify the current direct support cost funding model to a percentage of direct operational costs rather than a rate per metric ton.
7. **Recommendation 3.** Encourage and accept contributions specifically for direct support costs more transparently and with greater flexibility.
8. **Recommendation 4.** Move to a rolling three-year Management Plan with yearly approval.
9. **Recommendation 5.** Encourage and accept direct contributions to the Programme Support and Administrative budget on a case-by-case basis more transparently and flexibly.
10. **Recommendation 6.** Maintain the current indirect support cost model for funding the Programme Support and Administrative budget.
11. Following its discussion, the Board took note of the recommendations and requested further consultations. At an informal consultation in July, it was clear that there was not consensus with regard to the recommendations for allowing specific donor contributions for direct support cost (DSC) and Programme Support and Administrative (PSA) purposes. As a result, and because the practical applications and impact of these recommendations as well as recommendation 6 required further elaboration, the Secretariat removed these issues from the scope of the review.
12. The Secretariat also decided to consider recommendation 4, the implementation of a rolling management plan, in the context of a general review of the content and presentation

of the management plan, which the Board had requested during discussion of the WFP Biennial Management Plan (2010–2011) in November 2009. Any changes to the management plan cycle will therefore be proposed as results of that review.

13. This paper proposes changes to the WFP General Rules and Financial Regulations that will allow WFP to implement recommendations 1 and 2. The proposed changes would:
 - i) update WFP's costing model to incorporate non-commodity activities; and
 - ii) modify WFP's funding model to fund DSC on a percentage rather than a tonnage basis.

PROPOSED CHANGES

14. In 1996, WFP adopted the principle of full-cost recovery whereby donors are expected to meet all the operational and support costs of their contributions. This principle is outlined in General Regulation Article XIII.2:

“Except as otherwise provided in such general rules in respect of developing countries, countries with economies in transition and other non-traditional donors, or in respect of other exceptional situations, each donor shall provide cash contributions sufficient to cover the full operational and support costs of its contributions.”

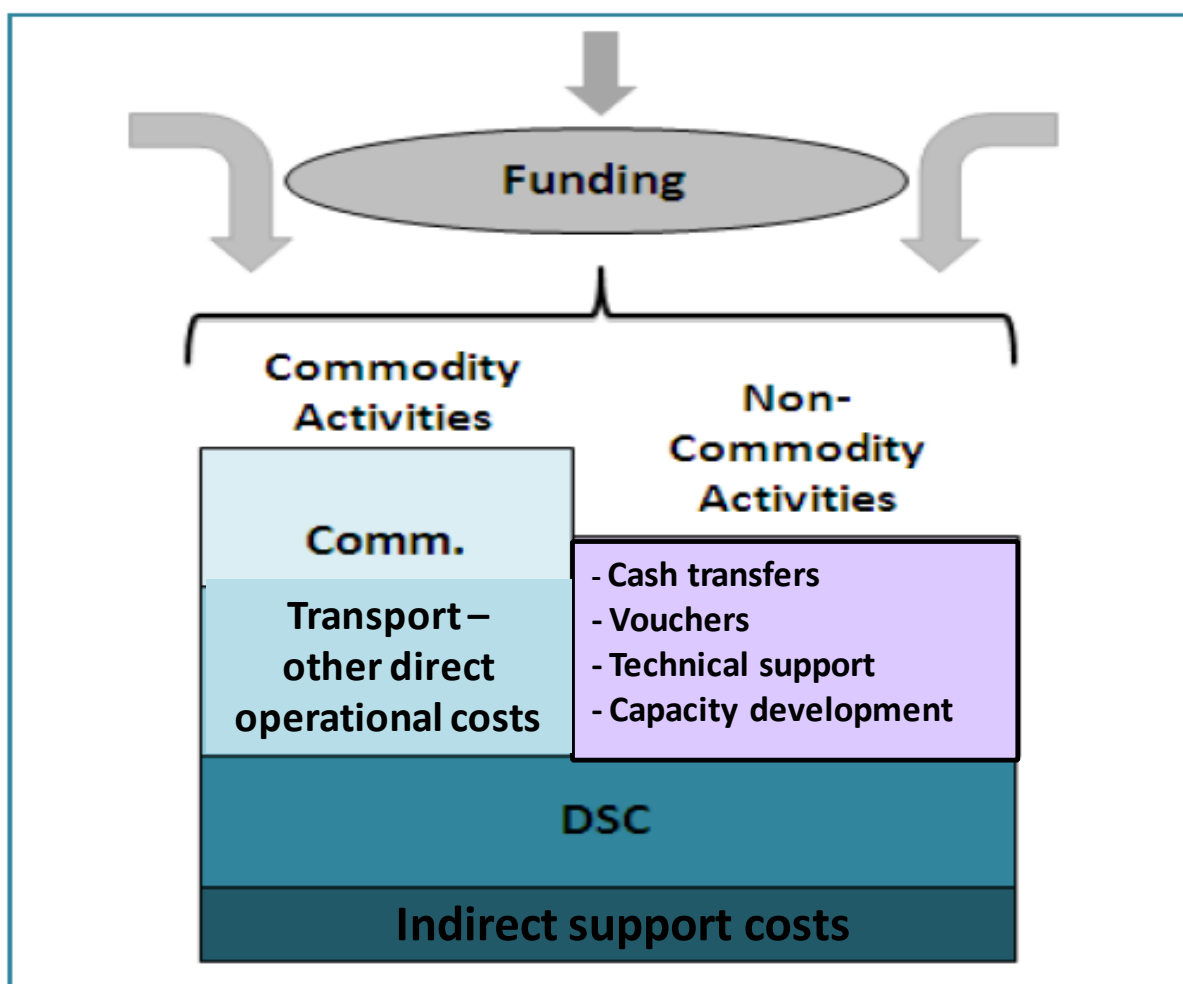
15. When this principle was adopted, it reflected the commodity-based assistance on which WFP focused, and provided a transparent and reliable way of ensuring that all WFP costs were covered, especially where in-kind commodity contributions or contributions designated solely for the purchase of a commodity were received. Consistent with this operational and funding environment, General Rule XIII.4 describes the calculation of full-cost recovery only in relation to the “commodity contribution”.
16. Although the principle of full-cost recovery is no less relevant today, there is an increasing demand to use contributions for non-commodity activities, such as cash and voucher transfers, local production of nutritionally enhanced food, and local capacity development, as outlined in the WFP Strategic Plan (2008–2013). As with commodity activities, such activities have costs that can be directly attributed to them and other costs that are related to them as part of the overall project support structure.
17. To ensure that the principle of full-cost recovery is transparently and equitably applied to all contributions to WFP, it is proposed to update WFP's financial framework to cater for non-commodity-based activities.

PROPOSED COSTING MODEL FOR NON-COMMODITY ACTIVITIES

18. Increasingly, WFP provides food assistance through means other than food distribution. Activities designed to promote access to nutritious food and protect livelihoods such as cash, vouchers, technical support and training play an increasingly important role in assisting beneficiaries and working with partners and are often combined with food distributions to achieve project goals.
19. The practice of embedding non-commodity activities in the commodity-based cost structure results in non-commodity inputs not being properly defined and categorized. This creates significant difficulties in planning, controlling, managing and implementing such activities. The practice also creates difficulties in benchmarking across projects, developing performance metrics and evaluating the impact of activities.

20. By implementing the following recommendation (Figure 1), the cost of non-commodity activities would be segregated within projects. This option would increase transparency, strengthen planning and management, and allow clearer links to performance indicators for all types of activities. The cost per mt of commodities would be easily identifiable, thus allowing for more accurate benchmarking and comparison of commodity-based activities across projects.
21. The approach would allow WFP to raise resources for commodity activities or non-commodity activities jointly or separately, depending on circumstances. WFP will continue to request contributions to a project as a whole, which empowers the project manager to implement the most effective and efficient activity at the time the contribution is received. However, recognizing that in some cases donors' interests and statutes may prohibit contributions to one or more types of activity within a project, contributions could be confirmed in part or in full for one or more specific activities. This approach would maximize WFP's ability to generate resources and maximize project impacts.

Figure 1: Segregate non-Commodity Activities and Allow Funding to the Project as a Whole or to Determined Activities



Recommendation 1: Segregate non-commodity activities within projects and – exceptionally – allow separate funding streams

PROPOSED FUNDING OF DIRECT SUPPORT COSTS

22. Direct support costs are those costs, generally at the country office level, that “can be directly linked with the provision of support to an operation and which would not be incurred should the activity cease”.¹ To calculate the DSC, recurring costs such as staff, vehicles, office rental and supplies, monitoring and evaluation, and training required are quantified and included in the project budget.
23. However, the DSC requirements are funded as a pro-rated share of the amount budgeted for a project, based on tonnage, as per General Rule XIII.4 (a). This approach creates the following:
- i) The funding availability for DSC for a given project can be variable and unpredictable, while the costs are relatively fixed, at least in the short term, resulting in significant planning difficulties.
 - ii) The broader and more complex nature of WFP’s food assistance means that the metric ton is no longer always the most appropriate indication of the size or complexity of an operation.
 - iii) The requirement that each donor fund DSC based on the tonnage provided does not necessarily result in a fair share of costs between donors when there are contributions for non-commodity activities.
 - iv) There may be a built-in incentive to engage in higher-tonnage activities.
24. At the Board’s 2010 Annual Session, the Secretariat recommended to “modify the current model [and use] DSC as a percentage of operational costs” as the basis for DSC funding. The Board took note of this recommendation and requested further discussion at an informal consultation. The informal consultation took place in July 2010, when there appeared to be consensus that the recommendation be adopted.
25. Under this recommendation, the DSC percentage in effect when contributions are confirmed would be applied to each contribution regardless of the intended use of the contribution. The DSC percentage would vary by project according to the demands of the project.
26. This approach has three major advantages: i) comparisons of DSC across projects will consider both commodity and non-commodity activities; ii) it allows DSC to be calculated equitably for all the donors providing resources to a project, whether for commodity or non-commodity activities; and iii) it removes the incentive to maximize tonnage purchases when more expensive commodities or non-commodity activities would be more effective.

Recommendation 2: Modify the current DSC funding model to a percentage of the operational budget rather than a rate per metric ton.

¹ WFP Financial Regulation 1.1.

Conclusion

27. The changes outlined here are fundamental for implementation of the WFP Strategic Plan (2008–2013). A clear, simple and transparent way of costing and funding non-commodity activities will provide the foundation for the shift from a food aid to a food assistance model of service provision. The change to the funding model for support costs will ensure an equitable cost apportionment for donors and a more stable provision of support to country offices.

PROPOSED CHANGES TO THE GENERAL RULES AND FINANCIAL REGULATIONS

28. General Rule XIII.4 (a) currently defines the calculation of other direct costs of a contribution as a “pro rata share of the budgeted costs ... based on tonnage”. For the implementation of recommendations 1 and 2 above, this wording poses two problems. First, there is no differentiation between direct support costs and other direct costs. Second, where a contribution is to be used for non-commodity activities, such as cash vouchers or capacity development, the full operational costs will be a monetary value only, thus there is no basis on which to calculate the value of direct support costs.
29. To implement the recommendations, the following changes are proposed to the General Rules:
- modify General Rule XIII.4 (a) to designate it more clearly as being only for commodity activities, and differentiate between other direct costs and direct support costs,
 - insert a sub-paragraph of General Rule XIII.4 to cover cash contributions not designated for commodity purchases; and
 - define the calculation of direct support costs for both commodity and non-commodity contributions as a percentage of the direct operational costs of the project.
30. In addition, the implementation of the above recommendations requires a broader definition of operational costs in Financial Regulation 1.1.

General Rule XIII.4

Current Text	Revisions (new text in underline)
<p>“In accordance with General Regulation XIII.2, the following shall apply to the various types of contributions to WFP:</p>	<p>“In accordance with General Regulation XIII.2, the following shall apply to the various types of contributions to WFP:</p>
<p>(a) Donors contributing food commodities or designated cash, such as cash in lieu of food commodities shall provide sufficient cash, acceptable services, or acceptable non-food items to cover the full operational and support costs related to their commodity contribution, using the following criteria for the calculation of operational and support costs;</p> <p>(i) commodities: to be valued in accordance with General Rule XIII.6;</p> <p>(ii) external transport: estimated actual cost;</p> <p>(iii) landside transportation, storage and handling (LTSH): average per ton rate for the project;</p> <p>(iv) other direct costs: pro-rata share of the budgeted amount for the project as in force at the time the contribution is made, based on tonnage;</p> <p>(v) indirect support costs: percentage of direct costs as determined by the Board.</p>	<p>(a) Donors contributing food commodities or designated cash <u>designated for food purchases such as cash in lieu of food commodities</u> shall provide sufficient cash, acceptable services, or acceptable non-food items to cover the full operational and support costs related to their commodity contribution, using the following criteria for the calculation of operational and support costs:</p> <p>(i) commodities: to be valued in accordance with General Rule XIII.6;</p> <p>(ii) external transport: estimated actual cost;</p> <p>(iii) landside transportation, storage and handling (LTSH): average per ton rate for the project;</p> <p>(iv) other direct <u>operational</u> costs: pro-rata share of the budgeted amount for the project as in force at the time the contribution is made, based on tonnage <u>average per ton rate applicable to the food component of the project;</u></p> <p>(v) <u>direct support costs: percentage of the direct operational costs of the project; and</u></p> <p>(↔) <u>(vi) indirect support costs: percentage of direct costs of the project, including direct operational costs and direct support costs, as determined by the Board.</u></p>
	<p>b) <u>Donors contributing cash designated for activities that do not include food distribution shall provide sufficient cash to cover the full operational and support costs related to their contribution, using the following criteria for the calculation of operational and support costs:</u></p> <p>(i) <u>direct operational costs: estimated actual costs;</u></p> <p>(ii) <u>direct support costs: percentage of the direct operational costs of the project; and</u></p> <p>(iii) <u>indirect support costs: percentage of direct costs of the project, including direct operational costs and direct support costs, as determined by the Board.</u></p>
FINANCIAL REGULATION 1.1	
Current text	Revisions
<p>Operational costs shall mean the costs of commodities, ocean transportation and related costs, landside transportation, storage and handling (LTSH), and any other input provided by WFP to beneficiaries, the government of the recipient country or other implementing partners</p>	<p>Operational costs shall mean <u>any costs, other than direct support costs or indirect support costs of WFP projects and activities.</u></p>

Revised Text:

General Rule XIII.4

“In accordance with General Regulation XIII.2, the following shall apply to the various types of contributions to WFP:

- (a) Donors contributing food commodities or cash designated for food purchases shall provide sufficient cash, acceptable services, or acceptable non-food items to cover the full operational and support costs related to their commodity contribution, using the following criteria for the calculation of operational and support costs:
 - (i) commodities: to be valued in accordance with General Rule XIII.6;
 - (ii) external transport: estimated actual cost;
 - (iii) landside transportation, storage and handling (LTSH): average per ton rate for the project;
 - (iv) other direct operational costs: average per ton rate applicable to the food component of the project;
 - (v) direct support costs: percentage of the direct operational costs of the project; and
 - (vi) indirect support costs: percentage of direct costs of the project, including direct operational costs and direct support costs, as determined by the Board.
- b) Donors contributing cash designated for activities that do not include food distribution shall provide sufficient cash to cover the full operational and support costs related to their contribution, using the following criteria for the calculation of operational and support costs:
 - (i) direct operational costs: estimated actual costs;
 - (ii) direct support costs: percentage of the direct operational costs of the project; and
 - (iii) indirect support costs: percentage of direct costs of the project, including direct operational costs and direct support costs, as determined by the Board.

FINANCIAL REGULATION 1.1

Operational costs shall mean any costs, other than direct support costs or indirect support costs of WFP projects and activities.