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**Executive Board  
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# UPDATE OF INDIRECT SUPPORT COST RATES

Agenda item 4 e)

## UPDATE OF INDIRECT SUPPORT COST RATES

**E**

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## NOTE TO THE EXECUTIVE BOARD

**This document contains recommendations for review and approval by the Executive Board.**

Pursuant to the decisions taken on the methods of work by the Executive Board at its First Regular Session of 1996, the documentation prepared by the Secretariat for the Board has been kept brief and decision-oriented. The meetings of the Executive Board are to be conducted in a business-like manner, with increased dialogue and exchanges between delegations and the Secretariat. Efforts to promote these guiding principles will continue to be pursued by the Secretariat.

The Secretariat therefore invites members of the Board who may have questions of a technical nature with regard to this document, to contact the WFP staff member(s) listed below, preferably well in advance of the Board's meeting. This procedure is designed to facilitate the Board's consideration of the document in the plenary.

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1. WFP retained the services of David M. Griffith and Associates, Ltd. - which had carried out previous cost studies - to conduct the 1997 Cost Study and analyse additional issues specified by the Board. The 1997 Cost Study is provided to the Board as document WFP/EB.3/4-E/Add.1.
2. The Cost Study applied a methodology consistent with that of previous studies. In general, the indirect support cost rates are the result of the programme support and administrative (PSA) costs attributable to each programme category (on the basis of a work measurement survey) divided by the total operational and direct support expenses, by programme category. The aim of the cost study was to determine the rates that should be applied to the total direct costs of projects (commodity value, transport, land transport, storage and handling (LTSH), and direct support costs) in order to generate resources to meet the PSA requirements as approved by the Governing Body.
3. The results of the 1997 cost study are shown in Table 1 below, together with those of earlier studies.

*Table 1*

<b>INDIRECT SUPPORT COST RATES BY PROGRAMME CATEGORY</b>			
(percent)			
	As per cost studies conducted in:		
	1997	1996	1995
Programme category			
Development	16.9	13.9	14.5
Emergency Operations (EMOP)	5.9	6.0	4.8
Protracted Relief Operations (PRO)	7.0	7.1	7.2
Special Operations (SO)	5.6	11.9	15.3
Average of all programme categories	9.1	8.6	8.1
Bilateral services			
Commodity procurement	6.8	4.0	3.1
Transport	12.8	4.5	4.7
Commodity procurement and transport	9.0	4.3	3.8

4. The rates calculated in the 1996 cost study were based on the work measurement survey for 1995, the approved 1996-97 budget and the estimated operational expenditures for 1996-97. The 1997 cost study was based on the work measurement survey for 1996, actual PSA and operational expenditures for 1996, and estimated PSA and operational expenditures for 1997. It should be noted that the rates increase, in comparison to the previous year's cost study results, if the attributed PSA for that programme category increases or the turnover decreases. Likewise, the rates drop if the PSA for a programme category decreases or the turnover increases.
5. For example, the rate for the Development programme category increased as a result of a reduction in operational expenditure with a concurrent increase in attributable PSA. Similarly, the rate for SO also changed because of a substantially higher level of turnover. The cost study gives detailed explanations on why each rate has changed from the prior year's rate. With respect to bilateral services, the rates in previous studies were based on



work measurement surveys covering the previous year; in these preceding years, the concept of bilateral services included what is now considered directed multilateral. With many of these bilateral services now identified as directed multilateral under the Resource and Long-term Financing Policies, the work effort associated with bilateral services results in the rates shown in Table 1.

6. It should be noted that the development rate is at the low end of the range of rates for similar organizations. The consultants point out in the study that “most other units of the UN System have a fixed rate of 13% of operational expenditures which they charge for support services to development projects; this represents only part of the costs these agencies incur.” The consultants’ report further states that studies conducted for other agencies with “rates computed using the same methodology for the costs of administrative and operational support services to projects ranged from 16% to 36%.” The Cost Study states that the artificially low rate of 13% may be applied because the difference is financed by these organizations’ Regular Budgets which are funded primarily from contributions by Member States.
7. The fluctuations of the rates reflect the inherent uncertainty of operating in an environment in which the level of turnover is unpredictable (especially in the case of emergency operations) and the inability to affect fixed costs in the short term. In 1995 and 1996, the rates calculated by the cost consultants were presented to the Governing Body for approval. When the approved 1997 rates (as per the 1996 Cost Study) are applied to the estimated operational expenditure in 1998-99, the revenue generated will not be sufficient; there will be a shortfall of \$23 million.<sup>1</sup> When the 1998-99 rates (as per the 1997 Cost Study) are applied, the shortfall will be \$12.9 million.
8. In order to fully recover the proposed PSA budget, the rates to be applied in 1998-99 require modification. Table 2 illustrates the different rates and the associated indirect support cost recovery shortfall for 1998-99.

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<sup>1</sup> All monetary values are expressed in United States dollars.



*Table 2*

**ALTERNATE INDIRECT SUPPORT COST RATES AND SHORTFALLS IN 1998-99**  
**WITH VARIOUS PSA AND TURNOVER ESTIMATES**  
**(percent)**

Programme category	Rates as per 1996 Cost Study	Rates as per 1997 Cost Study	Prospective rates for 1998-99 <sup>1</sup>
Development	13.9	16.9	17.7
EMOP	6.0	5.9	6.0
PRO	7.1	7.0	8.1
SO	11.9	5.6	8.5
Average	8.6	9.1	9.6
Biennial shortfall <sup>2</sup> (million dollars)	23.0	12.9	0

<sup>1</sup> The prospective rates for 1998-99, calculated by the cost consultants, are based on the same methodology and material upon which the updated rates were based, the only difference being the estimated turnover and the proposed budget. The bilateral rates are not affected.

<sup>2</sup> The shortfall is calculated by applying the rates to the projected 1998-99 operational expenditures.

9. Using the PSA of \$214 million and turnover of \$2,446 million, as projected in the 1998-99 WFP Biennial Budget (WFP/EB.3/97/4-A) would result in the rates shown in the third column entitled "Prospective rates for 1998-99" in Table 2 above. The prospective rate for the EMOP programme category remains relatively stable, but is higher for both PRO and Development, primarily because of a projected reduction of activities in these programme categories.
10. In order to slow down or reverse the trend of reduced resources for development activities, the Executive Board may wish to use part of the interest income for reducing the rate for the Development programme category. This action would be consistent with the practice of other United Nations organizations which use their Regular Budgets (financed from contributions by Member States) to reduce the actual rate. Alternatively, the Board may wish to use the interest income to reduce the rates in general. Several options are presented in the Annex.
11. With respect to the impact of multilateral contributions and the benefit of readiness, the results derived by the cost consultants showed only nominal cost differentials. With respect to the categorization of direct and indirect costs, the study found that there was no indication that costs charged as indirect were also being charged as direct. It recommends revising slightly the way in which costs are categorized. These issues may be reviewed further when the Secretariat analyses the effectiveness and applicability of the Resource and Long-term Financing Policies at the Executive Board's Annual Session of 1998.



12. Based on these observations, the results of the Cost Study and the recommendations of the cost consultants, the Executive Board is requested to:
- a) approve the indirect support cost rates for the biennium 1998-99;
  - b) adopt the rates for the biennium instead of for a single year to match the budget cycle (this convention would also alleviate the problem that an annual rate change creates for many donors who may go through a lengthy approval process for contributions only to have the rates change before the contribution is actually made); and
  - c) evaluate other relevant issues in the context of the Secretariat's review of the resource and long-term financing model and associated policies, to be presented to the Executive Board at its Annual Session of 1998.



## ANNEX



**INDIRECT SUPPORT COST RATES  
VARIOUS OPTIONS (percent)**

Option	Programme category				PSA shortfall	Basis of rates
	Development	PRO	EMOP	SO		
1	13.9	7.1	6.0	11.9	23.0	1996 Cost Study rates (Approved for 1997)
2	16.9	7.0	5.9	5.6	12.9	1997 Cost Study rates
3	17.7	8.1	6.0	8.5	0	Prospective rate: to fully recover PSA budget
4	9.6	9.6	9.6	9.6	0	Average rate for all programme categories to fully recover PSA budget
5	17.7	6.7	6.7	8.5	0	Option 3 (Prospective rate) with the rates for PRO and EMOP averaged
6	17.7	6.8	6.8	6.8	0	Option 3 (Prospective rate) with the rates for PRO, EMOP and SO averaged
7	14.0	6.4	4.7	6.7	0	Apportioning of \$44 million in interest income according to percent of PSA, by programme category
8	16.9	3.5	4.6	6.3	0	Apportioning of \$44 million in interest income according to interest earned, by programme category
9	16.0	4.1	4.7	6.6	0	Apportioning of \$44 million in interest income according to interest earned, by programme category (with interest earned by the General Fund attributed to Development)
10	15.2	5.2	4.6	8.5	0	Apportioning of \$44 million in interest income equally between Development, PRO and EMOP
11	7.6	7.6	7.6	7.6	0	Option 3 (Prospective rate) using \$44 million of interest income in aggregate
12	15.1	6.9	5.1	7.2	0	Apportioning of \$31 million in interest income according to percent of PSA, by programme category
13	17.1	4.9	5.0	7.0	0	Apportioning of \$31 million in interest income according to interest earned by programme category
14	16.5	5.3	5.1	7.2	0	Apportioning of \$31 million in interest income according to interest earned by programme category (with interest earned by the General Fund attributed to development)
15	15.9	6.0	5.0	8.5	0	Apportioning of \$31 million in interest income equally between Development, PRO and EMOP
16	8.2	8.2	8.2	8.2	0	Option 3 (Prospective rate) using \$31 million of interest income in aggregate
17	13.0	7.1	6.0	8.5	32.2	1996 Cost Study rates with the Development rate fixed at 13%
18	13.0	7.0	5.9	5.6	35.3	1997 Cost Study rates with the Development rate fixed at 13%
19	13.0	8.1	6.0	8.5	27.0	Option 3 (Prospective rate) with the development rate fixed at 13%
20	13.0	6.0	6.0	6.0	38.9	Simplified rates - interest income to subsidize Development, PRO and SO programme categories

