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# FINANCE COMMITTEE

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**Annual Report on Support Costs Expenditure and Recoveries**

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### EXECUTIVE SUMMARY

- This document reports on the application of the legacy policy for setting project servicing cost (PSC) rates, as well as on the new Cost Recovery Policy, approved by Council in 2015 and being implemented since 1 January 2018. The legacy and new support cost policies will run in parallel during the 2018-19 biennium. This report covers the period June 2017 to May 2018.
- During the period from 1 June 2017 through 31 May 2018, FAO opened 421 Trust Fund projects. Table 1 provides a categorized distribution of these projects in terms of support cost policy applied, the number of projects and the lifetime budgets. All projects have been charged at support cost rates envisaged by the legacy and new support cost policies respectively.
- The process of implementation of the new policy involved careful preparation over the past year, including development of guidance material, detailed instructions and training; communication and liaison with members and other resource partners; development of system supported processes; and follow-up, trouble-shooting and careful analysis of implementation issues.
- This document spans the final reporting period in which projects are approved under the legacy policy. Future reporting to the Finance Committee on this topic will be included as an integral part of the reporting on budgetary performance in the Annual Report on Budgetary Performance and Programme and Budgetary Transfers.

### GUIDANCE SOUGHT FROM THE FINANCE COMMITTEE

- The Finance Committee is invited to review the document and provide its guidance as deemed appropriate.

#### Draft Advice

##### **The Committee:**

- **took note of the application of the legacy policy for setting project servicing cost rates , as well as on the new Cost Recovery Policy for the period June 2017 - May 2018;**
- **recalled that the report presented spanned the final period in which projects would be approved under the legacy policy;**
- **welcomed the implementation of the new cost recovery policy since 1 January 2018;**
- and**
- **noted that future reporting on this matter would be integrated into the reporting on budgetary performance.**

1. This document reports on the application of the legacy policy for setting project servicing cost (PSC) rates, as well as on the new Cost Recovery Policy, approved by Council in 2015<sup>1</sup> and being implemented since 1 January 2018. The legacy and new support cost policies will run in parallel during the 2018-19 biennium. This report covers the period June 2017 to May 2018.

## I. Overview of the Cost Recovery Policies

### A. Legacy Policy

2. The legacy policy foresees the application of Project Servicing Cost (PSC) rates to extrabudgetary funded projects. The legacy policy continues to be applied to all projects which were ongoing as at 1 January 2018 as well as to those for which project formulation and negotiations with resource partners were at an advanced stage at that date.

3. The categories of extrabudgetary funded projects to which PSC rates apply as defined under the legacy policy are: technical assistance and direct support of Regular Programme (RP) activities, where a standard 13 percent rate is applied; and emergency assistance, where a ceiling rate of 10 percent is applied. The rate of PSC on jointly funded activities may vary between zero and 10 percent. The PSC rate may be reduced when the variable indirect support costs (as defined under the legacy policy) on a given project are expected to be lower. The function of appraising variations from standard PSC rates is entrusted to the Office of Strategy, Planning and Resources Management.

### B. New Policy

4. The new FAO policy on cost recovery foresees full proportional cost recovery. The methodology aims to closely reflect the actual costs of delivering a project, aligning with the inputs and operational conditions of individual projects and the actual support required.

5. The policy foresees a categorization of all FAO costs into Direct Operational Costs (DOC), Direct Support Costs (DSC) and Indirect Support Costs (ISC) as follows<sup>2</sup>:

- a) **Direct Operational Costs** - specific project inputs, such as personnel, equipment and supplies, travel, contracts, office space and transport, including FAO Technical Support, that are required for the full and timely delivery of project results;
- b) **Direct Support Costs** - FAO services needed to deliver specific project inputs, such as recruitment of personnel, organization and delivery of technical assistance, procurement of equipment and supplies, and the preparation of financial reports, as and when they occur. The DSC are recovered from individual project budgets through direct inputs or through cost pools using cost lists; and
- c) **Indirect Support Costs** - charged as a percentage of total direct costs to recover a project's share of the support expenditures incurred and which cannot be directly attributed to the implementation of specific project activities. ISC cover a share of management, governance and oversight, strategy and planning, audit and investigations, resource mobilization, partnerships, programme development, participation in UN Common Systems, outreach, advocacy and communications. The current ISC charge is 7 percent of direct project costs.

6. The process of implementation of the new policy involved careful preparation over the past year, comprising the following key elements:

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<sup>1</sup> CL 151/REP, paragraph 11 e)

<sup>2</sup> FC 156/7

- a) Development of guidance material, detailed instructions and an extensive training programme for colleagues involved in project formulation and implementation throughout the whole organization;
- b) Communication and liaison with members and other resource partners on the characteristics of the new policy as well as transition and implementation measures;
- c) Development of system supported processes for the management and monitoring of Direct Support Cost charges; and
- d) Follow-up, trouble-shooting and careful analysis of implementation issues, in order to allow prompt resolution.

### **C. Overview of support cost recoveries from 1 June 2017 - 31 May 2018**

7. During the period from 1 June 2017 through 31 May 2018, FAO opened 421 Trust Fund projects. Table 1 provides a categorized distribution of these projects in terms of support cost policy applied, the number of projects and the lifetime budgets. As anticipated to the Finance Committee in November 2017<sup>3</sup>, the reporting format has been revised to take account of the new policy coming into effect as of 1 January 2018.

8. The first section of Table 1 reports on projects approved under the legacy policy. All projects have been charged at support cost rates envisaged by the legacy policy, either through application of the standard PSC rates or through a combination of PSC percentage share and administrative and operational support as direct cost.

9. The second section provides an overview of the projects approved under the new policy. As of May 2018, the number of projects is still relatively few (total of 41 projects) but this number is expected to grow exponentially as we move through the 2018-19 biennium.

10. The third section provides an overview of the special categories, which fall under the flexibility that may be applied under the new cost recovery policy for special circumstances<sup>4</sup>. Projects funded by EU and GEF require FAO to follow their own budgeting and cost recovery guidelines. For emergency projects funded by UNOCHA, implementation of the new policy is deferred until January 2019 given the special nature of this fully decentralized resource partner. The interim period is being used to allow for the release of resource partner communication material, undertake country-level training and do a workflow review. TeleFood projects (which have a zero rate as per Conference Resolution 3/97) and a small number of other agreed special cases (mainly travel costs of participants from developing countries) are also included in this category.

11. The Committee is requested to note that this document spans the final reporting period in which projects are approved under the legacy policy. The purpose of this Annual Report was to provide a categorised distribution of PSC rates. Given that, under the cost recovery policy, one indirect support cost rate of 7 percent is applied irrespective of the type of project with direct support costs built into the individual budgets, the document in its current format is no longer relevant for future reporting. It is foreseen that future reporting will therefore be provided as an integral part of the reporting on budgetary performance<sup>5</sup>.

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<sup>3</sup> FC 169/8, paragraph 7.

<sup>4</sup> FC 161/6, Annex 1, paragraph 13.

<sup>5</sup> Including in the *Annual Report on Budgetary Performance and Programme and Budgetary Transfers* and the *Programme Implementation Report*.

**Table 1:** Distribution of the categories of support costs applied to projects opened June 2017-May 2018, by number and value

<b>Support Cost Category</b>	<b>Number of Projects</b>	<b>Lifetime Budget (USD '000)</b>	<b>% of Total Budget</b>
<b>1. Legacy Policy</b>			
Emergency assistance projects	92	289,308	
Technical assistance projects	103	241,022	
Projects in direct support of RP	42	31,503	
<i>Subtotal - legacy policy</i>	<i>237</i>	<i>561,832</i>	<i>61.3%</i>
<b>2. New Policy</b>			
Emergency assistance projects	31	46,144	
Projects in direct support of RP activities	6	5,775	
Technical assistance projects	4	22,862	
<i>Subtotal - new policy</i>	<i>41</i>	<i>74,781</i>	<i>8.2%</i>
<b>3. Special Categories</b>			
European Union	39	187,861	
GEF	30	37,852	
UNOCHA	30	53,182	
Telefood	36	315	
Other special cases	8	574	
<i>Subtotal - special categories</i>	<i>143</i>	<i>279,784</i>	<i>30.5%</i>
<b>Grand total</b>	<b>421</b>	<b>916,396</b>	<b>100%</b>