


TO: Heads of Departments/Offices  
A: Directors/Chiefs of Mission Support,  
Peacekeeping and Special Political Missions

DATE: 8 June 2012

REFERENCE:

THROUGH:

S/C DE:

FROM: María Eugenia Casar   
DE: Assistant Secretary-General, Controller

SUBJECT: **Cost recovery: programme support costs (PSC)**

OBJET:

1. In memoranda dated 20 July and 25 August 2011, my predecessor, Mr. Jun Yamazaki, established a working group on programme support costs (PSC). This working group was charged with developing a transparent and coherent policy on the application of PSC charges and the use of PSC revenue. It was led by OPPBA and included participants from OHCHR, UNOV/UNODC, UNOG, UNON, OCHA, DESA, ESCAP (for the Regional Commissions), DFS, DPA and Umoja.
2. The recommendations made by the PSC working group were formulated with the following understanding: (i) that the UN needs a clearer approach to the application of PSC charges; (ii) that we must work with the PSC formula approved by the General Assembly (in essence the 13% rate with controlled flexibility); (iii) that reduced PSC charges should not adversely impact average rates of cost-recovery; and, (iv) that the UN needs a clearer and more consistent approach to the allocation of PSC resources. The report of the PSC working group was endorsed by the UN's Chief Administrative Officers during their meeting on 20-21 March 2012.
3. It must be noted that a review of business practices is underway within the context of the implementation of the Umoja system. This will result in significant changes to the policies and procedures governing the management of trust funds and special accounts for programme support costs (with associated implications for ST/SGB/188 and ST/AI/284, ST/AI/285 and ST/AI/286). It is also anticipated that Umoja functionality will facilitate the computation of indirect costs. In this regard, the PSC policy defined herein will in due course be reviewed using appropriate Umoja capabilities. In the meantime, and in order to expedite the immediate implementation of a long-awaited PSC policy, I am hereby promulgating this policy by memorandum. I have applied the same approach to the issuance of a policy on service costs.

## Programme Support Costs

### Background, definition and purpose

4. The UN refers to the charge that it collects on trust fund (or “extrabudgetary”) expenditures as Programme Support Costs (PSC). The PSC charge is expressed as a percentage of direct costs. The recovery and use of PSC resources are of central importance to the financing and organization of efficient and effective programme support services.
5. In its decision 80/44 of 27 June 1980, the UNDP Governing Council approved a PSC rate of “13 per cent of annual project expenditures”. In its report on the PSC arrangements embodied in UNDP Governing Council decision 80/44, the ACABQ recommended that the UNDP formula be approved by the General Assembly for use by the United Nations Secretariat; this recommendation was accepted in resolution 35/217 of 17 December 1980 and remains in force. The UNDP formula allowed for a measure of flexibility as regards the granting of exceptions to the 13% PSC rate. In this context the schedule of rates defined below is intended to establish a transparent and consistent approach to the application of the 13% rate and justifiable reductions to this rate.
6. The purpose of the 13% PSC charge is to recover incremental indirect costs. Incremental costs are defined as the additional costs incurred supporting activities financed from extrabudgetary contributions. This charge is intended to ensure that the additional cost of supporting activities financed from extrabudgetary contributions is not borne by assessed funds and/or other core resources that are central to the budget review and approval process in the United Nations Secretariat.
7. Incremental costs can be divided into two basic categories, direct and indirect costs:
  - (i) Direct costs are those that can be readily and directly attributed to, and recovered, either wholly or in part, from an operation, programme or project financed from extrabudgetary contributions. Their definition requires that a direct link between the cost and project can be identified. These costs include but are not limited to: (i) substantive and operational staffing, facilities, equipment and activities<sup>1</sup> and (ii) programme services (planning, resource mobilization, monitoring, evaluation and management). They may also include direct costs pertaining to the administration of human, financial, physical and ICT resources (e.g. service costs). All direct costs should be financed by the relevant operation, programme or project.
  - (ii) Indirect costs are those that cannot be traced unequivocally to specific activities, projects or programmes. They include costs incurred by

<sup>1</sup> Including, for example, conference facilities, language and documents processing services

services providing administrative and other support functions to a range of operations, programmes and projects. These costs include but are not limited to: (i) the central administration of human, financial, physical and ICT resources; (ii) staffing, facilities, equipment, activities and legal liabilities related to (i) above; (iii) the implementation of UN-wide initiatives related to (i) above (e.g. Umoja and IPSAS implementation); and (iv) oversight (the Office of Internal Oversight Services and the Board of Auditors).<sup>2</sup> They may also include indirect (or overarching) costs pertaining to central programme services (planning, resource mobilization, monitoring, evaluation and management). Indirect costs are appropriately, and cost-effectively, recovered through the support costs charge expressed as a percentage of direct costs (i.e. by PSC).

8. In recent years UN organizations have taken steps, through the High-Level Committee on Management (HLCM) of the UN System's Chief Executives Board for Coordination (CEB), to harmonize the principles and definitions underlying their support costs policies. At a 26-27 July 2007 meeting of the CEB's Working Group on Support Costs, UNESCO presented the findings of a "comparative study of the cost recovery policies of several UN Organizations" in which it demonstrated that PSC rates were "converging towards 7%"<sup>3</sup>. In a 11 February 2009 progress report from the Chair of the Working Group on Support Costs it was noted that in April 2008, the Working Group had agreed that UN Organizations would apply a 7% PSC rate for Multi-Donor Trust Funds and multi-agency country level joint programmes and activities but that they could continue to apply standard indirect PSC rates up to 13% for single agency initiatives that are designed and managed directly/bilaterally. The 2011 report of the Secretary-General entitled "Civilian capacity in the aftermath of conflict" refers to the recommendation by a Senior Advisory Group convened to examine this issue requesting that "overheads charged by the Secretariat be aligned with the 7 per cent applied to multi-donor trust funds" and states that the UN will "examine the scope for aligning United Nations practices with those of other United Nations entities".<sup>4</sup>

#### New schedule of UN PSC rates

9. Bearing in mind experience gained over the years in implementing the 13% rate across the UN Secretariat's highly diverse range of substantive and support activities, it is clearly appropriate to rationalize, and implement, a simple readily understandable and transparent schedule of PSC rates, based upon clearly defined criteria. A series of rates will address the inflexibility of a single rate and the inherent lack of transparency associated with the granting of contribution-specific rates. A transparent PSC policy that requires fewer special arrangements provides greater

<sup>2</sup> It must be noted, for example, that the General Assembly, in its resolution 63/262 of 24 December 2008, endorsed a cost-sharing formula for the Umoja project which requires that 23% of project costs are borne by Special Accounts for Programme Support Costs.

<sup>3</sup> CEB/2008/HLCM/FB/3

<sup>4</sup> A/66/311-S/2011/527

assurances regarding the equal treatment of Member States and other donors. In this regard, the UN shall henceforth apply the following PSC rates:

- (i) 13% on all voluntary contributions where the UN retains primary and overarching programmatic responsibility and is the first or primary recipient of these funds. This is the rate endorsed by the General Assembly and it is critically important to the financing of programme support functions in numerous UN offices and programmes. A part of this rate may be shared with implementing partners where their costs cannot be properly identified as direct but at no point shall the aggregate PSC charge on operations, programmes or projects exceed 13%.
- (ii) 7% on all voluntary contributions in support of inter-agency and “Delivering As One” programmes and collaboration with other multi-lateral institutions where valid inter-agency arrangements apply. This rate is tied to valid inter-agency arrangements and may change as and when these arrangements change. The UN’s adoption of this rate responds to the Secretary-General’s pledge on 25 January 2012 to launch a new generation of the UN Delivering As One. It is intended to promote and foster inter-agency collaboration. The scope of this rate includes the modalities of the United Nations Development Group (including pass-through, pooled and parallel funding arrangements), Multi-donor Trust Funds and the Financial and Administrative Framework Agreement between the UN and the European Commission. A higher than 7% rate may still be accepted where inter-agency arrangements allow but at no point shall the aggregate PSC charge on operations, programmes or projects exceed 13%.
- (iii) 3% on all voluntary contributions for projects that are entirely implemented by other UN organizations, NGOs or government services (so called “pass-through arrangements”). This rate will apply when the UN Secretariat’s substantive responsibilities are restricted to project formulation, monitoring and evaluation and its administrative responsibilities are restricted to the acceptance and disbursement of funds and the recording of expenditures. Implementing partners may in turn ordinarily recover 7% but no more than 10% of their direct expenditure in order to ensure that the aggregate rate is no more than 13%.

10. It is anticipated that the 3 and 7% rates will largely replace, and provide clarity and consistency in respect of, current exceptions to the 13%. It should also be noted that the 13 and 7% rates will continue to be applied by the UN when comparatively minor components of an operation, programme or project are outsourced (i.e. using telegraphic and/or letter payment requests and grants). In certain instances, such as when specific activities entail additional and special support requirements, additional direct and indirect costs may be applied on a

case-by-case basis. Additional costs recognize that certain activities incur additional transaction costs and contend that the relevant operation, programme or project must assume direct responsibility for reducing, or financing, these costs. The application of appropriate additional direct and indirect costs will, for example, help assure Member States that the acceptance and use of contributions to which a less than 13% PSC is applied does not impose a burden of any type on regular budget resources and contributions that provide for the levy of the 13% charge.

11. Financial managers must monitor rates of recovery in the office or duty station for which they exercise delegated authority and take steps to ensure adequate cost recovery, including by ensuring that applicable direct service costs are levied against operations, programmes or projects financed from extrabudgetary contributions. The UN policy will not support the complete waiver of PSC charges. Exceptions to the new rates, apart from those referred to in paragraph 12, must be referred to me for approval together with detailed information explaining the technical justification for a special PSC rate and the adequacy of the proposed support provision(s).

12. The implementation of the above will take place immediately for all new contributions, agreements and arrangements. The PSC rates applicable to existing agreements and arrangements will apply until these agreements and arrangements are renegotiated. Where existing agreements and arrangements apply rates lower than those described above, they should be renegotiated in the current biennium (2012-2013) or else submitted to me for approval as an exception prior to 31 December 2013. It must be noted in this regard that the support costs modalities pertaining to the following arrangements will remain in force until further notice: (i) the United Nations Fund for International Partnerships where support costs are budgeted and financed directly; (ii) the Guidelines for the Preparation of Host Government Agreements Falling Under General Assembly Resolution 40/243 (ST/AI/2001/6 and ST/AI/342); (iii) Non-Reimbursable Loans of Personnel Services from Sources External to the United Nations Common System (ST/AI/231/Rev.1); and, (iv) UN associate expert programmes.

#### The use of PSC revenue

13. Programme support cost revenue is essential to the proper funding of support services and to ensuring that funds are used for the purposes for which they were provided. In this regard, the deployment of PSC within and between offices, programmes and departments must best address the operational, financial, human and other resources management challenges associated with extrabudgetary operations, programmes and projects. In accordance with the existing policy set forth in ST/AI/286, PSC income must be used in areas where a relationship exists between the supporting activity concerned and the activities that generated the programme support revenue.

14. Programme support cost revenue must be used where costs cannot be readily and directly attributed to, or recovered from, individual extrabudgetary

substantive activities, projects or programmes.<sup>5</sup> In this regard, PSC resources may be used to finance indirect costs under the following categories:

- (i) Central administration: staff in the human, financial, physical and ICT resources management areas that support operations, programmes and projects financed from extrabudgetary contributions; rent, maintenance, operating expenses, furniture and equipment relating to these staff.
- (ii) Central programme/departmental administration: staff in the human, financial, physical and ICT resources management areas that support operations, programmes and projects financed from extrabudgetary contributions; rent, maintenance, operating expenses, furniture and equipment relating to these staff.
- (iii) Other internally and externally provided services: IT, legal, security and oversight (the Office of Internal Oversight Services and the Board of Auditors); UN-wide initiatives (e.g. Umoja and IPSAS) and centrally managed charges.
- (iv) Programme/departmental programme services: central planning, resource mobilization, donor relations, monitoring, evaluation, reporting and programme development).

15. The cost-structures, operations, programmes, projects and corresponding PSC requirements of individual programmes/departments and administrative services vary considerably and it is therefore impractical to prescribe a universally applicable PSC apportionment formula. In this regard, PSC allocations will continue to be determined following case-by-case analyses, including, inter alia, of expenditure patterns, income projections, workload statistics and distribution and delegations of authority. Future PSC allocations to programmes/departments and administrative services shall allow for greater discretion in the use of these funds subject to the applications of the principles defined herein.

16. Decision making in respect of the distribution of programme support cost revenue between the categories defined above may correspond with one of two models:

- (i) Where Special Accounts for Programme Support Costs to which the PSC generated in support of the extrabudgetary activities of a particular department/programme are credited are managed by the Controller, or an official to whom the Controller has delegated this authority (i.e. a chief administrative officer in an office away from headquarters), the Controller or duly-designated official may allocate a portion to the programme/implementing office and retain a portion for central

<sup>5</sup> Support costs directly attributable to programmes and projects in field operations and offices may, for example, be classified and recovered as direct costs.

administration and UN-wide initiatives. All PSC funds must be used efficiently and effectively in support of relevant activities (i.e. in areas where a relationship exists between the supporting activity concerned and the activities that generated the programme support revenue). In respect of some departments/programmes an allocation may not be appropriate.

- (ii) Where the Special Account for Programme Support Costs is managed under authority assigned to a department/programme (i.e. an executive director of a UN Secretariat programme), the responsible central administrative service shall charge them for the human, financial, physical and ICT services they provide in support of their extrabudgetary operations, programmes and projects and shall substantiate these charges with workload statistics. The central administrative service shall also pass on charges for UN-wide initiatives and centrally managed charges (e.g. Umoja and IPSAS implementation). In the unlikely event that the department/programme and central administrative service fail to reach agreement on these charges, they shall refer them to the Controller for guidance and/or approval.