1. What are the practices in other UN organization regarding cost recovery mechanisms?

It is recalled that, as noted by IOS in its review of the Audit of UNESCO’s Cost Recovery (April 2020):

“(…) while management costs are recovered, those related to programme coordination and support are not. For example, the Bureau of Strategic Planning (BSP) is considered ‘management’ cost whereas functions such as Knowledge Management, External Relations & Public Information, and Management of Support Services are considered ‘programme coordination and support’. As a comparison with other UN organizations, it is relevant to mention here that the UNFPA cost recovery policy introduced in 2014 specifically includes functions such as corporate and external relations and partnerships, staff and premises’ security, field offices’ oversight, as management costs. “

The above results in under-recovery of costs that are currently funded by the regular assessed budget, and which should, in line with the objective of full cost recovery, be charged to donors.

It is also recalled that in order to ensure comparability and transparency for all stakeholders, and in line with Commitment #13 of the Funding Compact (A/74/73/Add.1–E/2019/14/Add.), UNSDG entities have agreed to develop a system-wide approach on cost definitions and classifications by 2021. For ease of reference, Commitment #13 in the Funding Compact states, ‘In consultation with respective governing bodies as appropriate, to improve comparability of cost classifications and definitions and enable greater transparency across time and between United Nations Sustainable Development Group entities.’ This work is currently ongoing under the aegis of the High Level Committee on Management’s Finance and Budget Network. Certain changes to the classifications of UNESCO’s costs will be proposed in line with these efforts in order to ensure better alignment with the rest of the UN common system.

Elements of these cost classification related changes will already be proposed as part of UNESCO’s cost recovery policy revision but will not entail any financial impact beyond what is proposed currently through the introduction of the POC, which includes 1% for the CSI Special Account.

All UN Organizations agree on the principle of full cost recovery as outlined by the QCPR, i.e., “full cost recovery and proportionality, from core and non-core resources, thereby avoiding the use of core or regular resources to subsidize activities financed by non-core or extra-budgetary resources”. A number agencies have taken initiative and already harmonized their Cost Recovery Polices, and have come to recover similar types of costs even if the mechanism in place may be different from one organization to another dependent of the funding modalities, etc. And for the recovery of indirect costs, many organizations are using more than one method of charging. Some have already implemented the principle of full cost recovery. UNESCO agrees with the principle of full cost recovery and has been working accordingly in order to avoid subsidizing voluntary contribution funded projects through the regular assessed budget.
However, the regular assessed budget has been still covering a large proportion of certain
costs related to project implementation (maintenance, utilities, supplies, security, UN
machinery, etc.), thus subsidizing the projects funded by voluntary contributions. The new
policy intends to strengthen the principle of full cost recovery by introducing a Post Occupancy
Charge, using the proportion of staff costs, thus ensuring proportionality in funding these costs
between the regular assessed budget and voluntary contributions, at the same time ensuring
to avoid double-charging of the same cost items.

The key elements of the cost recovery policy of some of the selected UN common system
organizations are presented in the Annex I. to the present document.

2. What is the calculation method for the POC and the expected amount to be charged
on VC projects compared to the current mechanism?

The POC rate will be established on the basis of costs which are necessary for programme
delivery, but which are not charged as direct costs nor are recovered currently through the
PSC rate. These items include maintenance and utility costs, security costs, running costs, IT
licenses and some of the Joint UN Machinery contributions. The costs that are intended to be
recovered from voluntary contribution projects are those that are not currently charged directly
to the projects, therefore the POC does not incur double charging of the same items. The
latest actual expenditure trend for these items is being analyzed, and the POC rate shall be
defined in combination with the expected staff costs under the voluntary contribution, i.e. the
calculation methodology is intended to:

(i) identify the total actual costs to be recovered under the POC based on actual
expenditures in 2018/2019/2020;

(ii) divide these costs by the total personnel costs for the same period (fixed term,
temporary, and special service contracts); and

(iii) the resulting percentage will become the charge to be applied to the standard
costs of personnel costed under project budgets for all voluntary contribution
funded activities. The standard costs will be the basis for costing personnel budget
and no separate percentage charge needs to be applied.

3. What is the expected rate which would apply as POC? Would it be in addition to the
8% PSC, the 1 % levy charged on tightly earmarked funding, and the staff costs
recovery? When will the POC be applied to regular funding?

Based on preliminary results of the ongoing analysis, the POC rate is expected to come out
to be around 9% of the project personnel cost. This rate shall be applied only on the personnel
costs under the voluntary contribution projects (and, unlike the PSC rate, not on the total costs
of the projects). As an indicative information, globally speaking, this POC to be charged to the
voluntary contribution personnel costs would correspond to only around 2% of the total project
expenditure.

It is recalled that while the POC will be an additional charge for the donors compared to what
they are currently paying, the costs being recharged to donors are not new or additional costs.
They have been paid by the regular assessed budget to date. Furthermore, the fees
mentioned above are targeted at charging/recovering different costs. The summary table
below illustrates the costs incurred in the process of implementing voluntary contribution
funded activities, and the sections below provide further details in response to the questions raised.

(i) The costs recovered under the PSC (or management cost rate) of 8%, are targeted at recovering the costs of “management”. As defined, these include costs relating to the functions whose nature of support is cross cutting and whose primary purpose is to promote the identity, direction and well-being of the Organization. Management costs are recovered from the project support costs charged to extrabudgetary projects, using the principle of proportionality. As defined under the revised 2018 policy, they include:
- Direction
- Human Resources Management
- Bureau of Financial Management
- Bureau of Strategic Planning
- Management of Information Services and Communication

As noted above, the policy revision may involve some element of restructuring of the costs being recovered.

(ii) The 1% "levy" charged on tightly earmarked funding is a charge applied by the UN Secretariat directly at the source of funding (UNESCO never sees this money) to contribute to the new RC system. In the long run, the levy is also expected to help to incentivize a shift to more pooled, thematic and joint funding mechanisms as called for in the 2016 QCPR.

(iii) The total charges for a donor (depending on the purpose and type of donation) will therefore be comprised of the following, which will be funded from the donation itself:
- Direct project costs, including staff cost recovery where relevant;
- Management costs – charged through the PSC (average 8% on project expenditure incurred);
- Programme delivery related costs – charged through the POC as part of the standard cost of personnel (around 9% of personnel cost to cover utility, security, running costs etc., including 1% for the CSI Special Account); and
- The 1% levy charged by the UN on tightly earmarked funds is in addition to the above, but in no way contributes to recovering any of UNESCO’s costs.

(iv) The staff costs charged to projects to recover staff time spent by non-project expert resources are referred to as “staff cost recovery”. There is no “fee” per se being charged for these, rather the estimated cost of the time of individuals spending time on projects is charged directly, based on standard costs. The 2% “target” is an aspirational objective to be achieved as an overall percentage of staff costs, based on an estimate that at least this much of staff time (other than direct project resources and management time) is spent on facilitating and contributing to the implementation of voluntary contribution funded activities.

(v) The POC will be applied only on the personnel costs funded by voluntary contributions. UNESCO will examine the possibility of applying the POC to the regular budget in the future (as does WHO), but this would involve a broader restructuring of the way common costs are charged and is not contemplated at this time.

See also the summary table of costs incurred and recovered in Annex II.
4. **What would be the scope of application of the POC on non-earmarked funds and Category 1 Institutes?**

POC will be charged on both earmarked and non-earmarked voluntary contributions. However, further consultations are envisaged with Category 1 Institutes to assess the feasibility and applicability of charging POC on their personnel costs. At this stage, we assume that these charges are unlikely to be applied by Category 1 Institutes and UNESCO Brasilia Office, as their recovery model differs somewhat from that of the rest of UNESCO. The final detailed policy proposal will make specific reference to the applicability of the changes to Institutes and the UNESCO Brasilia Office, and will take due account of consultations on this subject.

5. **What mechanism would be put in place to finance and strengthen properly the field offices?**

The POC charges in respect of voluntary contribution funded activities in HQ will be credited to the units which incur these expenses (ADM/Operations; ADM/Knowledge Management, etc), while the charges in respect of such activities in the field will be credited to the Field Offices that incur these for their future activities. This will also help to compensate for the perceived shortcoming of the current cost recovery policy in place since April 2018, whereby Field Offices are no longer receiving the PSC income.

6. **Clarification is requested regarding the inclusion of the POC in the standard costs - paragraph 14 indicates that it is only for voluntary contributions, but the decision does not specify this.**

POC shall be included in the standard costs so that it will be correctly reflected in the initial budget information for all voluntary contribution funded projects. The decision may of course be amended in this regard if Member States wish to see this explicitly therein. As the intention was to keep this phase of the decision at the level of principles, and subject to the approval of the detailed policy at the next EB session, this level of detail was not specified in the proposed draft decision.

7. **How would the Secretariat ensure that there is no cross subsidization from the Regular Programme to Voluntary funded projects?**

As indicated above, the objective of the policy review is to continue to pursue full cost recovery, which is in line with the QCPR. By reviewing the different types of costs incurred in support of UNESCO’s operations, and targeting the recovery of the appropriate costs that contribute to delivery and support of voluntary contribution funded activities, the Organization will be able to continue to improve the proportion of costs recovered. The changes contemplated to the policy, e.g. the introduction of the POC, aim at this also.

8. **Would the POC mechanism simplify the review of VC budget proposals for donors?**

Not necessarily simplify, but it would not make the budget proposals any more complex either, as the result of the change in policy will simply require a change in the costing of personnel costs. No added complexity would be introduced in the budget proposals.
9. How would the introduction of a Post Occupancy Charge impact the review of the targeted cost-recovery rate for staff costs in voluntary contribution-funded projects (currently 2% as an Organization-wide goal).

Introduction of POC is independent of the staff cost recovery (please see also response to Question 3 above).

10. What type of reporting would be presented on the application of the POC, the exceptions, the funds collected and their use?

It is intended that the POC application, recovered amounts and their use will be reported to Member States in the periodical Financial Management Reports. The calculation of the POC would be regularly reviewed and updated in order to ensure that the cost recovery remains aligned with the actual costs incurred.

11. How would the cost recovery ratio between voluntary and regular funding be affected by the POC?

One of the aims for introducing POC is to realize a fairer cost sharing between the regular budget and voluntary contributions. Today, a significant level of costs related to supporting voluntary contribution funded activities is still funded primarily by the regular budget. POC will enable voluntary contribution (staff costs) to contribute certain magnitude of amounts to these costs.

12. Overall, how much funding could the POC generate for UNESCO?

As the POC rate is still being analyzed, a preliminary estimate would be that at the current level of expenditures, each 1% of POC on voluntary contribution personnel costs could be expected to recover $0.9M per biennium. Accordingly, a POC of 9% would generate around $8M for the biennium, part of which will be transferred to the CSI.

13. What will be the impact of revising the proportion of funding from RP and VC for the income of the Management Cost Account?

Based on the most recent actual expenditure figures, the funding ratio RP/VC for the Special Account is expected to be modified to 56/44 from 63/37 used in the 40 C/5. This means that the Special Account will be funded relatively more by VC in the next biennium. If the total amount of Special Account to be utilized for 41 C/5 were to be at the same level as 40 C/5, it would mean that approximately $6-7M would be switched from RP to VC.

14. If 63% of the Special Account revenue was from the regular programme budget – should not the same proportion of the residual balance remain in the regular budget?

The Special Account operates as an independent account in order to fund all costs of the Management Services. Therefore, once the RP funds and VC funds are transferred into the Special Account, it should be considered that the funds belong to the Special Account, and no
longer to RP or VC. It is also recalled that most of the surplus of the Special Account last biennium was due to interest income from VC funds.

15. **Would a better distribution of indirect costs between RP and VC lead to a reduction in the RP budget? By what amount? If the RP budget does not decrease, how can it be ensured that the RP amounts will be allocated to activities?**

The improved distribution of costs between RP and VC arising from POC is supposed to lead to a reduction in the RP budget in the medium to long term. However, initially, we will need to be prudent by monitoring the actual evolution of recovery by POC, and the budget structure can reflect the POC impact on RP budget once the POC recovery becomes stable and robust.
**Annex I: Key elements of cost recovery policy of UN Organizations**

<table>
<thead>
<tr>
<th>UN Organization</th>
<th>Income Resources (funding structure)</th>
<th>Cost Definition and Classification</th>
<th>Cost Recovery contributes to the following costs</th>
<th>Charge rate (in addition to direct charges)</th>
<th>Remarks</th>
</tr>
</thead>
<tbody>
<tr>
<td>UNICEF (UNDP, UNFPA, UN Women)</td>
<td>100% Voluntary contributions - Other Resources (3/4) - Regular Resources (1/4)</td>
<td>1. Development activities - Programmes - Development effectiveness 2. Management 3. UN Development Coordination 4. Special Purpose 5. Internal oversight and evaluation</td>
<td>Separation between HQ and Country Level. HQ: Executive direction, external relations fund raising and partnerships, corporate communications, legal oversight audit, corporate evaluation, information technology, finance, administration, security and human resources. Country Level: Staff Cost: Operation’s manager, Human resources, Administration, Finance and Information communication and technology. Non staff costs: Utilities, Office premises/equipment office supplies, miscellaneous services related to maintenance of office premises.</td>
<td>PSC 8%</td>
<td>45 – 50% of the Institutional budget (non programme) is covered by the cost recovery.</td>
</tr>
<tr>
<td>WFP</td>
<td>100% Voluntary Funding</td>
<td>Transfer costs - Implementation cost - Direct support cost - Indirect support cost</td>
<td>1. Strategy and Direction 2. Services to Operations 3. Governance independent oversight and fundraising</td>
<td>PSC 6.5%</td>
<td>Introduction of Programme Support and administration Budget equalization fund (P8A)</td>
</tr>
<tr>
<td>WHO</td>
<td>6 budget categories (5 programme, 1 corporate services) Category 6: Corporate services and establish Services</td>
<td>Leadership and Governance, strategic planning and resource coordination; strategic communications; accountability, transparency and risk management; and management and administration</td>
<td>PSC 13% POC: 9.5%</td>
<td></td>
<td></td>
</tr>
<tr>
<td>UNHCR</td>
<td>98% Voluntary Earmarked and Un-earmarked Assessed and Voluntary Contributions</td>
<td>Programme Costs (PG) Programme support costs (PS) Management and Administration Costs (MA)</td>
<td>Management, Procurement, finance, HR, IT, Donor relations and other indirect activities</td>
<td>ISC = 6.5% for Earmarked funds</td>
<td>As of 1/1/2020</td>
</tr>
<tr>
<td>FAO</td>
<td>Full recovery form Regular programme and extra-budgetary (IBF)</td>
<td>Direct operating Costs (DOC) – any costs relating to specific inputs. Direct Support Cost (DSC): those that can be attributed to supporting the provision of specific inputs Indirect Support Costs (ISC): support the execution of the delivery of activities.</td>
<td>Direct support Cost: HR services, Procurement services, financial services &amp; services. Indirect Support Costs: Policy, executive direction and management, governance and oversight</td>
<td>ISC: 7% to all projects from Regular programme and extra budgetary delivery DSC: to be identified and budgeted</td>
<td>BF: New policy, One ISC rate for all projects (7%) Rate to be reviewed every two years</td>
</tr>
</tbody>
</table>
### Annex II: UNESCO's Cost Recovery Elements Summary

<table>
<thead>
<tr>
<th>Cost of VC project</th>
<th>who pays /how currently</th>
<th>as proposed (subject to further refinement and discussion in the course of finalizing the policy)</th>
</tr>
</thead>
<tbody>
<tr>
<td>staff cost directly and only involved in implementing the project (PA, SC), including its different components (ASHI, Termination costs etc...)</td>
<td>donor - should be clearly specified in project budget set out in the agreement</td>
<td>no change</td>
</tr>
<tr>
<td>travel, training, licenses, other costs of staff related strictly and only to the project</td>
<td>donor - should be clearly specified in project budget set out in the agreement</td>
<td>no change</td>
</tr>
<tr>
<td>cost of goods and services for the project specifically, including IPAs and consultants, vehicles and other items purchased purely for the project etc., audit, evaluation</td>
<td>donor - should be clearly specified in project budget set out in the agreement</td>
<td>no change</td>
</tr>
<tr>
<td>cost of premises, utilities, maintenance etc that can not be directly attributed to the project but are incurred costs that also directly serve the project. This also includes costs that are currently excluded from &quot;central services&quot; but which actually also support activities funded from VC (UN joint machinery, etc.)</td>
<td>mostly RP budget - premises costs may have host country contribution (in Field, where they provide premises), and some projects may allow inclusion of part or all costs in the project budget. RP bears all costs of UN joint machinery and certain non-central services that benefit ALL activities regardless of source of funding. donor is envisaged to pay through POC. Costs that are covered by generosity of host country will not be charged in the POC. Where these types of costs can be considered as direct costs, they will be charged directly to the project budget, otherwise they will be charged through the POC (there will be no double charging).</td>
<td>no change</td>
</tr>
<tr>
<td>cost of central services</td>
<td>cost of central services shared between RP and donors - RP currently pays 63% while 37% comes from the Management Cost Rate (or PSC) of 8% average.</td>
<td>No change on the PSC rate. The RP share will be adjusted (reduced) to reflect the actual proportion of UNESCO's funding.</td>
</tr>
<tr>
<td>cost of program specialists, staff experts who contribute to the management, coordination, advice etc. needed for the project, which can be directly charged back to the project based on the time they spend working on the same</td>
<td>Staff costs are RP costs, although some are charged to donors, but not all that could be charged are charged. Currently about 2% of staff costs are recharged to VC through this mechanism, but a more systematic and careful charging methodology is expected to result in a notable increase in this percentage.</td>
<td>Target increase recovery of staff time from VC</td>
</tr>
</tbody>
</table>