

Note to the IASC Working Group and Emergency Directors Group

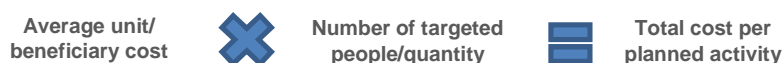
Summary of Activity-Based Costing Study and HPC Steering Group's Recommended Next Steps

1. On behalf of the IASC Humanitarian Programme Cycle Steering Group, OCHA commissioned a study on the application of activity-based costing for budgeting strategic response plans by an independent external team, composed of Abby Stoddard and Barnaby Willitts-King. The report was completed in August 2014 and aims to inform IASC discussions without prescribing specific recommendations for action or institutional/procedural changes. The desk review looked at activity-based costing in a sample of countries: Afghanistan, Central African Republic, DR Congo, Haiti, Yemen and Zimbabwe. The occupied Palestinian territory and South Sudan were also included as two countries that considered applying this approach before resuming with coordinated project planning.

Activity-based costing country ¹	Year of the appeal/SRP	Part of study	Projects after appeal/SRP launch
1. Afghanistan	2013-2014	Y	Funded projects on FTS
2. Central African Republic	2014	Y	Projects on OPS for peer review (deferred)
3. DR Congo	2007-2014	Y	Funded projects on FTS
4. Haiti	2013-2014	Y	Projects on OPS for peer review (deferred)
5. Iraq	2014	N	Projects on OPS for peer review (deferred)
6. Myanmar	2014	N	Funded projects on FTS
7. Yemen	2014	Y	Projects on OPS for peer review (deferred)
8. Zimbabwe	2011-2012 (only)	Y	Funded projects on FTS

Source: OCHA/PSB as of August 2014.

2. Activity-based costing refers to a method of estimating overall funding requirements using average costs per sectoral activity, multiplied per person (or unit), and then added together to present the total resources needed per cluster. This approach represents a departure from the way funding requirements for inter-agency plans have been calculated traditionally through coordinated project planning (i.e. by adding up the budgets of individual projects). The review team found that no single definition or approach encapsulates activity-based costing at present. There were significant variations in the methodology used by clusters to do activity-based costing, making objective comparison between them difficult. In each case, country cluster coordinators independently developed a tailor-made approach for their cluster. As a result, what is called activity-based costing actually encompasses a number of different methods. In addition, the level of quality and rigor varied across cases and across clusters. With the exception of Afghanistan, most clusters were not able to provide the review team with a written methodology or set of formulas for how they derived their cost estimates.



Factors to consider in costing per beneficiary/unit: type of beneficiary targeted, phase of programme, transport and logistics, security, access, procurement source, distribution channel, staff, training, indirect/overhead costs, etc.

3. A common driver for those contexts adopting activity-based costing was a desire to revitalise coordinated humanitarian action and restore credibility to response planning in the eyes of both donors and participants. Activity-based costing was perceived to lead to better, more needs-driven resources mobilization than the supply-driven nature of project planning. Additionally, cluster partners expressed frustration with the labour-intensive project planning process, with no 'return' on their investment. Activity-based costing was considered to lighten the administrative workload in the early stages of the planning process and present a clearer picture of the expected cost.

¹ 2014 preliminary/strategic response plans for Pakistan, Ukraine, Colombia and Turkey (all not publicly released) have also used an activity-based costing approach.

4. In the application of this approach, there were a few common issues among the case study countries. Clusters reported too little time and/or guidance to fully understand and develop a comprehensive methodology for activity-based costing. The underlying objectives of the shift to activity-based costing were not always clear or commonly understood at the outset. Despite this, a majority felt that the approach had value as an innovation in strategic response planning. The additional time afforded by not having to produce project sheets and vet them allowed more space for a response planning process that felt more inclusive and strategy-focused according to those interviewed. For those countries that undertook coordinated project planning as a second step to activity-based costing (sometime referred to as 'deferred' project planning), the work was undertaken later, on a less compressed timetable. When coordinated project planning was dropped altogether, there was concern about accountability and transparency of funding and operations, and this demanded increased OCHA and cluster capacity to be able to match donor funding to planned activities. In terms of funding, coverage of requirements in DRC, Zimbabwe and Afghanistan appeared to be higher, but this could not be directly attributed to the activity-based costing approach in any definitive way; for CAR and Yemen it was deemed too early to say.

Activity-based costing

* Potential advantages

Strategic/effectiveness gains	Coordination/efficiency gains	Information/ accountability gains
<ul style="list-style-type: none"> • More cohesive and sector-focused planning and prioritisation • Rapid application in sudden-onset crises 	<ul style="list-style-type: none"> • Less time pressure and lighter administrative burden • Flexibility to allow for changing conditions and responses 	<ul style="list-style-type: none"> • A clearer 'whole picture' estimate of resource needs, unobscured by multiple projects of different scales and scopes of coverage

* Potential disadvantages

Quality/effectiveness losses	Coordination/ participation losses	Information/ accountability losses
<ul style="list-style-type: none"> • Weaker quality control with loss of project review/vetting in the planning phase • Loss of project-related quality assurance tools such as the gender marker 	<ul style="list-style-type: none"> • Less government engagement in cluster planning process • Loss of NGO visibility, threatening equal opportunity to donor funding 	<ul style="list-style-type: none"> • Less transparency, if projects are not later listed in FTS/OPS (and a lack of incentive to do so if funding is received prior to project submissions)

5. The review team identified several potential advantages and disadvantages to activity-based costing. A summary is included in the graphic above. The views among different stakeholder groups seemed to vary considerably. UN agencies expressed concern over the loss of projects (when deferred project planning did not follow activity-based costing) as leading to losses in quality (vetting)² and accountability (project monitoring and financial tracking). There was also worry about unfavourable comparisons if their project budget was to show a higher cost per beneficiary than the overall sectoral estimate. The agencies saw a risk that the estimated costs would be used by donors as benchmarks to drive costs down inappropriately and without an understanding of variables. Global clusters wanted to be better included in the application of the approach at the field level, and some expressed concern that activity-based costing may not be a workable method for their cluster's budgeting. None of the NGO representatives who were consulted expressed any opposition to an activity-based costing approach, or even a sense of wariness in terms of their visibility in strategic response plans or accessibility to direct donor funding. No host government representatives were included in the study, but anecdotal information indicated that government representatives in the six cases have not raised significant obstacles to activity-based costing; the review team queried whether the loss of projects may make governments feel a loss of control in knowing where agencies were planning to carry out activities. Donors did not seem closely engaged or informed of the approach, and gave no sense of a

² A GenCap advisor is conducting a study on the feasibility of transforming the gender marker for use in monitoring and evaluation and generally how it could work beyond the project level.

strong preference either way. Where donors have been engaged, they have been supportive of the potential transparency and objectivity of using activity-based costing and the visibility implications of removing projects was not of great concern to donors interviewed.

6. The study concluded with a number of necessary 'ingredients' for an activity-based costing model to work. A few are referenced here. Sufficient time, support, guidance and tailoring to the context and across clusters are needed to allow buy-in. Global and country level clusters need to 'own' the approach to be effective, including ensuring consistency within the clusters on key principles of unit cost methodologies. When activity-based costing is practiced, some type of project planning is still required, particularly to allow for activity and financial tracking. Improvements or alternatives to OPS and FTS need to be considered to support tracking of funding in a more flexible way. OCHA and cluster capacity in-country needs to be sufficient to be able to properly implement this approach, particularly with respect to information management capacity to track details on funding and response activities for transparency and accountability. In short, activity-based costing represents a significant change in the way strategic response plans are constructed, and with this change comes the challenge of learning a new way of doing business.
7. The study underscored that overall awareness and knowledge of activity-based costing is limited, which undermines "sensible discussion". It noted that many views on activity-based costing are coloured by a partial understanding of what it means, or by theoretical objections rather than ones borne out in practice. Activity-based costing is often erroneously associated with the removal of project planning altogether. Likewise, a common understanding of the specific intended results or outcomes of the new approach does not yet exist, making it difficult to objectively measure success or failure in any particular case. As a result, the desk review relied mostly on qualitative information and participant perceptions to identify positive and negative indicators that suggest potential future advantages and risks.
8. Given that more information needs to be collected to clarify the overall approach and further develop the methodological aspects, the IASC Humanitarian Programme Cycle Steering Group **recommends** the following action:
 - (a) Circulate the report with a note to those HCs/HCTs already applying an activity-based costing approach (see accompanying note). They should be encouraged to document their process/data used to calculate costs for transparency and accountability purposes and be advised of any pitfalls to the approach as highlighted in the study.
 - (b) Refrain from encouraging other countries to switch to an activity-based costing approach until more data is gathered. For the same reason, it was also felt that it would be premature to broadly disseminate the report at this juncture.
 - (c) Establish an inter-agency group – inclusive of global clusters and cluster lead agencies to further study the potential of activity-based costing and/or other possible costing methodologies, including improvements to coordinated project planning. The group should focus on this issue from a (technical) response planning perspective.
 - (d) Request OCHA and the global clusters to proactively collect more information in the current planning cycle from those countries applying the activity-based costing approach. This information should be provided to the inter-agency group (recommended in point c) to inform their discussion and to attempt to 'codify' the approach.