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JOINT MEETING

**Joint Meeting of the
Ninety-sixth Session of the Programme Committee
and the
Hundred-and-fifteenth Session of the Finance Committee**

Rome, 27 September 2006

Funding of the General Service Salary Increase in 2006-07

This document is submitted for discussion to the Joint Meeting of the Programme and Finance Committees

The Secretariat invites Members of the Committees who may have questions of a technical nature with regard to this document to contact the FAO staff focal points indicated below, preferably well in advance of the meeting.

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EXECUTIVE SUMMARY AND DRAFT RECOMMENDATIONS

1. The International Civil Service Commission (ICSC) has recommended a new salary scale for the General Service category of the Rome-based organizations reflecting a 12.16% increase. Part of the increase was budgeted in the PWB 2006-07 to become effective in November 2005, but the extent of the increase was unforeseen at the time the Conference approved the PWB 2006-07. The unbudgeted cost for 2006-07 is US\$ 12.6 million plus US\$ 1.3 million for two months in 2004-05, for a total of US\$ 13.9 million.
2. The ICSC recommendations have been submitted through the Finance Committee to the Council for approval in November 2006. Payment to staff will need to be effected as soon as possible thereafter, with assurance of the necessary financial coverage. The Secretariat has identified three possible options, or combination of options, for dealing with the unforeseen additional salary costs:
 - a) Utilize the contributions to the 2006-07 programme of work of the Russian Federation, which became a Member of FAO in April 2006. This important but also exceptional event requires decision on the treatment of Russia's contributions in 2006-07, which will amount to approximately US\$ 7.5 million. The Committees could recommend to the Council that this resource, unforeseen at the time when the Conference approved the PWB 2006-07, be used to meet partially the unforeseen General Service salary increase. A precedent for dealing with unexpected additional contributions exists and arose when, after the PWB process for the next biennium was almost completed, it appeared that a number of new Members would join FAO after the level of the PWB had been decided. The Conference at the time agreed to treat the amounts as Miscellaneous Income, to be used to cover unexpected expenditures.
 - b) Charge the unforeseen salary costs (or portion thereof, in case the above proposal to fund part of the expenditure from Russia's 2006-07 contribution is approved) to the Special Reserve Account in accordance with applicable resolutions. However, the reserve also has other ongoing purposes and has undergone significant depletion in recent years. A charge to the SRA would lack any source of funding without replenishment by Members of the SRA of at least an amount equivalent to the charge. Replenishment of the SRA to its authorised level of 5 percent of the effective working budget of the Organization was last approved by Conference in 1991. Considering the purposes of the SRA for protection of the PWB as provided in the resolutions and the general depletion which the reserve has undergone in the intervening years, it may in fact be advisable and financially prudent to seek Conference approval for replenishment to the authorised level, which for 2006-07 would be US\$ 38.25 million.
 - c) As a last resort course of action, some degree of adjustments to the programme of work.
3. The Committees are requested to consider the details of the options, and recommend a course of action for Council approval.

A. INTRODUCTION

4. The International Civil Service Commission (ICSC) has recommended a new salary scale for the General Service category of the Rome-based organizations reflecting a 12.16% increase, to be effective 1 November 2005 (see FC 115/16 Recommendations of the ICSC and the UNJSPB). Part of the increase was budgeted in the PWB 2006-07 to become effective in November 2005, but the extent of the increase was unforeseen at the time the Conference approved the PWB 2006-07. The overall financial impact in 2006-07 of the introduction of the new scale is US\$ 19.7 million, and the unbudgeted cost for 2006-07 is US\$ 12.6 million plus US\$ 1.3 million for the two months in 2004-05, for a total of US\$ 13.9 million.

5. The ICSC recommendations have been submitted through the Finance Committee to the Council for approval in November 2006. In line with the requirement of the Salary Survey methodology to freeze interim adjustments that fall due during the six months prior to a survey and which was due in November 2005, no salary increase has been paid to headquarters General Service staff since November 2004. Payment to staff will need to be effected as soon as possible thereafter, with assurance of the necessary financial coverage. The Secretariat has identified three possible options, or combination of options for dealing with the unforeseen additional salary costs, i.e. the contributions of the Russian Federation to the 2006-07 programme of work, the Special Reserve Account and, as a last resort course of action, adjustments to the programme of work.

B. POSSIBLE SOURCES OF FUNDING

Contributions of the Russian Federation to the 2006-07 programme of work

6. On 11 April 2006 the Russian Federation, a State eligible for original membership of FAO, accepted the Constitution of FAO, in accordance with its Article XXI, paragraph 1. Membership of the Organization became effective on that date. This important event is also exceptional because no provision is made in the Basic Texts regarding the initial assessment of a nation eligible for original membership, which becomes a Member upon deposit of an instrument of acceptance of the Constitution. Indeed, the provisions of the Basic Texts regarding contributions by new Member Nations concern situations where an additional Member is admitted under Article II, paragraph 2 of the Constitution, as a result of a decision of admission to membership by the Conference. Specifically, General Rule XIX, paragraph 3, states that “*the first contribution of an additional Member Nation (...) shall be determined by the Conference at the time of its decision on the application for membership*”. In addition, Financial Regulation 5.8 provides that “*any nation admitted to membership (...) shall pay a contribution to the budget for the financial period in which the membership (...) becomes effective. Such contributions shall be an amount determined by the Conference and shall begin with the quarter in which the application was approved. All new Member Nations shall be required to make advances to the Working Capital Fund (...)*”.

7. The instrument of acceptance of the Constitution was received and took effect on 11 April 2006, i.e. after adoption by the Conference of the Scale of Contributions for 2006-07. Therefore, it is not now possible to change the Scale of Contributions for the current biennium. Still, as Russia’s membership was unforeseen at the time when the Conference approved the 2006-07 PWB, it is now necessary to decide how Russia’s contributions for 2006-07 should be treated.

8. As part of its broad advisory functions on all financial matters, the Finance Committee is, *inter alia*, required to keep under review the Scale of Contributions and to submit recommendations to the Council regarding any modification of such scale. In addition, in view of the exceptional, one-time nature of a matter with potential impact on Regular Programme

assessments of all Members and on the implementation of the PWB 2006-07, it is proposed that the Finance and Programme Committees should consider and recommend an option for treatment of Russia's contributions, for approval by Council.

9. The Russian Federation's contribution to FAO represents 1.106 percent of the Scale as calculated with the methodology based on the applicable United Nations Scale of Assessments, as approved by the FAO Conference. Since the Russian Federation's membership became effective as of April 2006, its obligations for the year 2006 amount to US\$ 1.46 million and Euro 1.47 million, equivalent to three quarters of the total assessed contribution for the year. For 2007, the sums due will amount to US\$ 1.95 million and Euro 1.96 million. On a biennial basis, expressed in US Dollars at the budget rate, Russia's contribution is about US\$ 7.5 million for 2006-07. The obligation of the Russian Federation in respect of its advance to the Working Capital Fund is US\$ 276,500.

10. The Secretariat proposes for the Committees' consideration the following option for the treatment of the Russian contribution.

11. By becoming a Member of FAO, the Russian Federation is required to discharge its main obligation attached to membership, which is to make a contribution to the budget, as per a number of provisions of the Constitution and the Financial Regulations. Although the Conference, at its last session, could not apportion a share of the budget for the Russian Federation, it would not be legally incorrect to consider that the contribution of the Russian Federation should be treated as a contribution to the budget. The Committees could recommend to the Council that this resource, unforeseen at the time when the Conference approved the PWB 2006-07, be used to meet partially the unforeseen General Service salary increase. Two observations could be made in relation to this proposal:

- first, it could be seen to imply exceeding the level of the budgetary appropriations for 2006-07, and related authority to spend by the Director-General, as voted by the Conference in accordance with the provisions of Article XVIII of the Constitution and Financial Regulation 4.1(a). However, it should be pointed out that such appropriations were voted in order to allow the implementation of a programme of work, which needs to be preserved as far as possible, and the additional resources would be used to finance unforeseen expenditures required for the implementation of the planned programme of work, for which the appropriations were voted. In addition, the proposed course of action would be of an exceptional nature - required to deal with a matter that has never arisen in this manner in FAO and which is not contemplated in any legal provisions, thus warranting an ad hoc treatment of the matter.
- second, consistent with this suggestion, which would allow the Organization to partially cover the unforeseen consequences of the introduction of a new General Service Salary Scale, it would be open to the Committees to conclude that the contribution by the Russian Federation should not involve a reduction of the assessment of other Members in respect of the biennium 2006-07.

12. In view of the above, consideration could be given to treating the contributions from the Russian Federation, in respect of 2006 and 2007, as Miscellaneous Income. This approach would better respond to the above concerns regarding the level of the approved budgetary appropriation, as well as the implications of the contribution in respect of the assessed contributions of other Members. In this connection, the Committees may wish to note a precedent of direct relevance to the issue at hand. At its Autumn Session, in 1959, as it appeared that a number of States would be admitted to membership by the Conference, the Finance Committee was of the view that, for various reasons, including the unforeseen receipt of a large number of applications shortly before the Conference, at the time when the PWB process for the forthcoming biennium was almost completed, it would be appropriate to treat the contributions of the new Members for the biennium 1960-1961 as Miscellaneous Income. Therefore, it recommended that, "*as an*

exceptional measure, the contributions of the new Member Nations (...) should not be included in the Scale of Contributions for 1960-61 but should be additional to the scale of assessments and should accrue to Miscellaneous Income, of the Organization for 1960-61". The Conference, after having noted that such contributions would be used to cover some "unexpected expenditures", approved this course of action, and noted that the contributions of the new Members would, of course, be included in the new Scale of Contributions for 1962-63. Drawing on this precedent, the Committees could recommend to the Council that the contributions from the Russian Federation be treated as Miscellaneous Income, and thereby used to cover a portion of the unforeseen General Service salary increase.

Special Reserve Account

13. The SRA account was established by Conference in 1977 and its purpose was expanded by Conference Resolutions 13/81 and 17/89. The reserve's purpose is (1) to protect against the effects of unbudgeted costs arising from fluctuations in exchange rates and to record realised gains and losses on exchange; (2) to advance funds to the General Fund to finance budgetary expenditure pending receipt of contributions (when the Working Capital Fund is insufficient); and (3) to finance unbudgeted costs of approved programmes due to unforeseen inflationary trends (subject to prior review and approval of the Programme and Finance Committees).

14. Resolution 13/81 specifies that the SRA should be maintained at a level equivalent to five percent of the total effective working budget of the Organization, which in 2006-07 would represent US\$ 38.25 million. The previous replenishment by special assessment on Member Nations was authorised by Conference in 1991 (Resolution 16/91), for an amount of US\$ 28 million.

15. In the intervening years the SRA balance has fluctuated with the net effects of currency variances but has generally declined, and stood at US\$ 10.3 million at the end of the 2004-05 biennium (as of that date the SRA had also been advanced in full to the General Fund so as to mitigate the Organization's recourse to external borrowing). As reported in the Audited Accounts 2004-05, the SRA has undergone depletion of US\$ 14.7 million last biennium. Analysis of the exchange gains and losses charged to the SRA has shown that the main cause of the exchange differences recorded is delays in receipt of Members' contributions¹.

16. In 2006 the SRA has undergone further depletion to absorb exchange losses due mainly to the delays in payment of Member Nation contributions, and the current balance stands at approximately US\$ 8 million. Considering that a pattern of delays in payment of Member contributions seems likely to recur, the Organization remains exposed to the currency effect of delays in Member contributions in 2006-07 and the SRA would be needed to continue to provide coverage of exchange losses in the course of 2006-07.

17. Furthermore, the SRA balance has been advanced in full to the General Fund in accordance with applicable resolutions which require the temporary use of reserves before recourse to external borrowing. Such borrowing became necessary in June 2006 due to the magnitude of unpaid Members' contributions, and will likely be required for the rest of the year. Once sufficient assessed contributions are received, external borrowing will be extinguished and the reserves restored.

18. Considering that the extent of the increase in General Service salaries resulting from the ICSC survey was unforeseen, the conditions for use of the Special Reserve Account, in accordance with the SRA resolution's provisions concerning unbudgeted extra costs due to unforeseen inflationary trends, are met. Such use requires prior approval by the Finance and Programme Committees and was in fact the source identified in 1998-99 to cover additional

¹ This residual risk under split assessments was reported in 2003 (FC 102/INF/18 para 15) and in the report to Conference (C 2005/16 paras 13, 14, 19) on the performance of split assessments in 2004-05.

remuneration of US\$ 1.9 million to General Service staff following the ILOAT ruling on recognition of the language factor.

19. The Secretariat submits that the unforeseen and unbudgeted General Service salary increase for 2006-07 (or portion thereof, in case the above proposal to fund part of the expenditure from Russia's 2006-07 contributions is approved) could be charged to the Special Reserve Account in accordance with its resolutions. However, a charge of additional unforeseen salary costs to the Special Reserve Account would lack any source of funding without at least an equal amount of replenishment of the SRA through a special assessment on Members. It would thus be prudent to foresee the necessary financial coverage to be provided by SRA replenishment from Member Nations special assessments of at least an amount equivalent to the charge. Should the proposal to utilize Russia's 2006-07 contributions of US\$ 7.5 million to partially cover the unbudgeted costs be accepted, the SRA replenishment to be proposed to Conference would amount to US\$ 6.5 million.

20. In fact, it would appear to be timely and cautious to seek replenishment of the SRA, considering several years of depletion to cover exchange losses. In order to provide means to fulfil the three purposes of the Special Reserve Account noted in paragraph 13 above, the Secretariat requests the views of the Finance and Programme Committees on the replenishment of the SRA to the extent foreseen in Conference Resolution 13/81, which is a level of five percent of the effective working budget of the Organization. For 2006-07 this would represent US\$ 38.25 million. Considering that the SRA balance at the end of 2004-05 was US\$ 10.3 million, a special assessment of US\$ 28 million could be put forward for Conference approval in 2007.

Programme Reductions in 2006-07

21. Should the membership not approve the above sources, or combination thereof, to secure the necessary funding, the impact on the Organization of the unforeseen and thus unbudgeted General Service salary increase would imply an equivalent degree of reductions in the approved programme of work. This eventuality needs to be considered in the context of:

- the impact of the near ZNG budget level for the biennium of US\$ 765.7 million, which required the Organization to absorb, through further efficiency savings and programme cuts, US\$ 39 million in cost increases (equivalent to a real reduction of 5.2% over the previous biennium);
- the need to cover other unbudgeted expenditure in 2006-07 estimated at US\$ 16 million as described below; and
- the need to incur during 2006-07 part of the US\$ 15.2 million one-time costs of implementing the reforms approved by the Conference.

22. Aggregate adjustments of such magnitude cannot but have a serious impact on the delivery of outputs and services for Members when compared with the activities of the Organization in 2004-05.

23. In providing their endorsement of the revised programme of work at the approved 2006-07 budget level, the Committees expressed concern that certain priority areas might not be adequately funded. In effect, the Programme Committee identified support to the IPPC, plant and animal genetic resources, food safety, agricultural water management, GIEWS, the corporate statistical database FAOSTAT, and support to implementation of the Code of Conduct for Responsible Fisheries as areas which should be protected during implementation. The Committee: *"requested that allotments to these priorities not fall below the budgeted amounts, and that they be considered for any savings that could arise from the implementation of decentralization."* The Finance Committee, for its part, took particular note of the potential adverse impact on internal financial controls, which will need to be addressed *inter alia* through increased provisions for the Local Audit Programme, the Finance Division and the Office of the Inspector-General.

24. When setting the allotments for implementation of the programme of work, the secretariat must also take account of potential unbudgeted and under-budgeted costs which may require funding during the biennium. The main areas of under-budgeting for the current biennium are presently estimated at US\$ 16 million (2.1% of the approved budget) relating mainly to staff costs: increases in salaries and pensions (not including the GS salary increase recommended by the ICSC for the Rome-based organizations), higher medical insurance coverage, and unfavourable exchange rate fluctuations for posts outside headquarters, as well as redeployments costs due to the reduced budget. Based on the current allotments, the managers of affected programmes are already making adjustments to their resource mix and work plans to accommodate the unbudgeted costs, with unavoidably negative impact on outputs and services.

25. Adding the unbudgeted cost of the GS salary increase of US\$ 13.9 million would bring the required allotment reductions for the biennium to US\$ 30 million (3.9% of the approved budget). Should the membership not approve alternative sources of funding, priority-based protection would be applied at programme entity level, as was done when issuing updated 2006 allotments in June 2006.

26. Thus, if feasible, absolute protection would have to be provided to the priority areas highlighted by the Programme Committee, described above. In addition, specific areas indicated by the Conference would continue to be fully protected (TCP, Capital Expenditure and Security Expenditure), as well as incompressible costs (external audit, national liaison offices), internal controls and internal audit. These areas account for US\$ 176 million (23%) of the budget, so the cuts would fall particularly hard on the other areas of the programme of work, amounting to an average 5.1% reduction (on top of an overall real reduction of 5.2% over the previous biennium). They would undoubtedly entail the need for freezing posts. It is also recalled that, pending further voluntary contributions from Members, part of the one-time costs of implementing the reforms approved by the Conference would require funding from the 2006-07 programme of work.

27. In synthesis, enforcement of further reductions of up to US\$ 14 million over the remainder of the biennium (to cover unbudgeted general service salary increases at headquarters) would fall largely on "unprotected" programmes which are nevertheless considered very important by most members, and increases the risk of making many of them unviable in the biennium. The loss of outputs and services cannot be assessed precisely at this stage, as this would require communicating to FAO units more precise priority-based reduction targets and receiving their proposals, a premature action while awaiting Governing Body guidance. The impact would be substantial and the Secretariat submits that this should be considered as a last resort course of action. Pending a decision by the Council on the means of funding, the unbudgeted cost of the GS salary increase has not been factored in the Implementation of the Conference Decisions and Proposals from the Director-General (document CL 131/18). Should this prove necessary, the substantive outputs which would have to be cancelled or postponed, and the areas of reduced policy and technical advice to Members, would be duly indicated in the next Programme Implementation Report.

28. The Committees are requested to consider the details of the options presented above, and recommend a course of action for Council approval.