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FINANCE COMMITTEE

Hundred and Thirty-eighth Session
Rome, 21 - 25 March 2011
2010 Actuarial Valuation of Staff-Related Liabilities

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EXECUTIVE SUMMARY

- This document updates the Finance Committee on the results of the actuarial valuation of the Organization's liability for staff-related plans (the "Plans") at 31 December 2010.
- Section ***I. Introduction*** describes the Plans, which provide distinct benefits to staff either on completion of service or as a result of work-related illness or injury. It also explains the purpose of annual actuarial valuations.
- Section ***II. Results of Actuarial Valuation*** summarises the total liability of the Plans as at 31 December 2010, 2009 and 2008 and provides the key assumptions used in those valuations. During 2010 the total liabilities of the Plans increased by USD 39.0 million from USD 1,110.8 million at 31 December 2009 to USD 1,149.8 million at 31 December 2010. This increase is primarily attributable to the rise in the After Service Medical Coverage (ASMC) liability and the rise was broadly in line with expectations. The reasons for the increase are explained in more detail in paragraph 3.
- Section ***III. Current Financial Situation*** provides the total recorded, unrecorded and net balance sheet liabilities for the Plans based on the actuarial valuations, as well as the total funded and unfunded liabilities for the Plans as at 31 December 2010, 2009 and 2008, respectively. The total unfunded liability of the Plans as at 31 December 2010 was USD 824.9 million compared to USD 805.9 million at 31 December 2009.
- Section ***IV. Accounting and Funding*** provides a comparison of the annual Current Service Costs for the Plans for the three years ending 31 December 2011. The Current Service Cost for 2011 is USD 35.0 million (2010 – USD 31.2 million). This section also includes full funding proposals for the ASMC plan and Terminal Payments Fund (TPF). The annual past-service ASMC funding amortization to fully fund the liability by 2040 amounts to USD 25.5 million, while the funding approved by Conference for 2010 and 2011 amounted to USD 7.0 million per year leaving a shortfall of USD 18.5 million per year. The annual past-service TPF funding amortization to fully fund the liability by 2025 amounts to USD 5.3 million for which no funding has ever been approved.
- Section ***V. Comparison with other UN organizations*** provides the Committee with a table comparing the status of the After Service Medical Coverage liabilities at various UN agencies.

GUIDANCE SOUGHT FROM THE FINANCE COMMITTEE

- The Committee is invited to note the results of the 2010 actuarial valuation and the current financial situation, accounting and funding of the Organization's liability for staff-related plans at 31 December 2010. The Committee is invited to report to Council the biennial funding amounts necessary to fully fund the liabilities by 2040 (ASMC) and 2025 (TPF).

Draft Advice

- **The Finance Committee notes the amounts necessary to fully fund the ASMC and TPF past service liabilities by the target years of 2040 and 2025, respectively, and agrees that these amounts should be reported to Council for consideration in the draft Programme of Work and Budget 2012-13. The Finance Committee makes specific note of the following points:**

  1. **The growth in the value of the overall liability for after-service benefit plans has stabilized owing to several refinements made to the actuarial calculation over the past few years; and**
  2. **The ASMC liability remains seriously under funded. In the case of the TPF, no funding sources of past service liability have ever been approved and, therefore, any TPF payments in excess of the budgetary provision for current service cost will increase the structural cash deficit of the Organization.**

Introduction

1. FAO has four staff-related plans (the "Plans") that provide benefits to staff members either upon completion of service or as a result of work related illness or injury. The Plans are as follows:

- **Separation Payments Scheme (SPS)** –According to the provisions of this plan the General Service category staff at Headquarters are entitled to receive a separation payment equivalent to 1/12th of the staff member's Final Net Annual Salary Rate multiplied by years of service between 1 January 1975 and 31 December 1990, plus 1/13.5th of the staff member's Final Net Annual Salary Rate multiplied by years of service after 1 January 1991.
- **Termination Payments Fund (TPF)** – The Termination Payment Fund comprises benefits payable to staff upon separation from service, specifically Repatriation Grant, Repatriation Travel and Removal, Commutation of Accrued Leave, Termination Indemnity, and where applicable, Death Grant.
- **After Service Medical Coverage (ASMC)** – is a medical insurance plan for retired staff and their families meeting certain eligibility criteria. The Basic Medical Insurance Plan provides partial reimbursements for certain hospital, physician, dental, psychiatric, physical therapy, hospice and eyeglass charges subject to various limits and exclusions. The premium of the Basic insurance is nominally shared between the retired staff member and the Organization.
- **Compensation Plan Reserve Fund (CPRF)** – The Compensation Plan provides benefits subject to certain limitations to staff members (including, *inter alia*, consultants and persons holding Personal Service Agreements) in the event of injury, illnesses, or death attributable to the performance of official duties. The benefits include annuities or lump-sum payments (supplementing the UN Pension benefits, if applicable) in the event of death or disability, and reimbursement of reasonable medical, hospital and directly-related expenses.

2. All of the above Plans are treated by the Organization as defined benefit plans. To meet the financial reporting requirements the Organization annually obtains from an external actuarial firm a valuation of all the Plans in order to:

a) determine the Organization's overall liabilities associated with the Plans;
b) establish the annual expense related to the Plans' maintenance;
c) quantify recommended rates of contributions to fully fund the liabilities; and
d) obtain information necessary to meet financial reporting requirements.

The actuarial valuations for 2010, 2009 and 2008 were performed by Aon Hewitt (www.hewittassociates.com).

The results of 2009 actuarial valuation of the Plans were reported to the Finance Committee in April 2010[1]. This document refers to the results of the actuarial valuation as at 31 December 2010 and the current financial situation, and accounting and funding of the Organization's liability with comparative information as at 31 December 2010, 2009 and 2008.

[1] FC 132/3 *2009 Actuarial Valuation of Staff Related Liabilities.*

Results of Actuarial Valuations

3. A comparison of the total actuarial liability by plan as at 31 December 2010, 2009 and 2008 is detailed in Table 1.

Table 1

(in USD Millions)		Increase/ (Decrease)			Increase/ (Decrease)		
Plan	**31.12.2010**	***USD m***	***%***	**31.12.2009**	***USD m***	***%***	**31.12.2008**
CPRF	17.6	*(0.4)*	*-2.2%*	18.0	*(2.5)*	*-12.2%*	20.5
TPF	60.8	*2.6*	*4.5%*	58.2	*7.6*	*15.0%*	50.6
SPS	88.8	*(11.3)*	*-11.3%*	100.1	*6.6*	*7.1%*	93.5
ASMC	982.6	*48.1*	*5.1%*	934.5	*56.9*	*6.5%*	877.6
Total actuarial liability	**$1,149.8**	***39.0***	***3.5%***	**$1,110.8**	***68.6***	***6.6%***	**$1,042.2**

4. As detailed in Table 1 above, the net increase of USD 39.0 million in the actuarial liability between 31 December 2010 and 31 December 2009 was mainly due to a rise in the ASMC liability of USD 48.1 million coupled with a decrease in the SPS of USD 11.3 million. The variation in the ASMC liability can be analysed as:

Increases totaling USD 149.8 million, comprised of:

- expected net change in the liability of USD 44.5 million related to accrual of current service and interest cost for 2010, less actual benefit payments;
- change in discount rate from 5.4% to 5.0% of USD 65.5 million;
- change in participation and spousal coverage at retirement of USD 30.4 million;
- miscellaneous demographic experience as compared to previous actuarial estimates of USD 8.3 million; and
- new hires during 2010 of USD 1.1 million.

Decreases totaling USD 101.7 million, comprised of

- movement in EUR-USD exchange rate of USD 57.4 million;
- claims and administrative expenses experience of USD 41.1 million; and
- benefit payments different than expected during 2010 of USD 3.2 million.

The reduction in the SPS is mainly due to movements in the EUR-USD exchange rate of USD 8.7 million.

5. The actuarial valuation of the Plans requires the Organization to make certain assumptions in order to best estimate the cost of providing these benefits to its staff members. Such assumptions include demographic (e.g. mortality rates/estimates, rates of staff member turnover, claim rates under medical plans, etc.) and financial (e.g. discount rate, future salaries and benefits, future medical costs, etc.). Owing to changes in factors, both internal and external, the Organization, together with the actuaries, performs an annual review of the assumptions used in the actuarial valuation and adjusts them where it is deemed necessary for a more accurate calculation of the Plan liabilities. Like most actuarial calculations, annual valuations are subject to significant uncertainty and unpredictability. In particular, the values of the Organization’s liabilities for the Plans are highly sensitive to changes in the EUR-USD exchange rate, the discount rate, and medical claims and anticipated medical inflation. For the purpose of 2010 actuarial valuation there were no significant changes in the basis of the actuarial assumptions. The key assumptions used in the valuations of the Plans for 2010, 2009 and 2008 are presented below in Table 2.

Table 2

Key Assumptions	2010	2009	2008
Economic			
1 Discount rate			
ASMC	5.0%	5.4%	5.6%
SPS	4.7%	5.1%	5.6%
TPF	5.3%	5.8%	5.6%
CPRF	5.5%	5.9%	5.6%
2 Medical cost inflation rate	5% starting from 2011	6% during 2010, and 5% thereafter	7% during 2009, 6% during 2010, and 5% thereafter
3 General inflation rate	2.5% per year	2.5% per year	2.5% per year
4 Year end spot rate €/USD	1.31	1.44	1.43

Current Financial Situation

6. Table 3 and Graph 1 below show the total recorded and unrecorded liabilities[2] for the Plans based on the actuarial valuations, as well as the total funded and unfunded liabilities[3] for all Plans as compared to the fair market value of earmarked long-term assets[4] at 31 December 2010, 2009 and 2008, respectively.

Table 3

(in USD Millions)

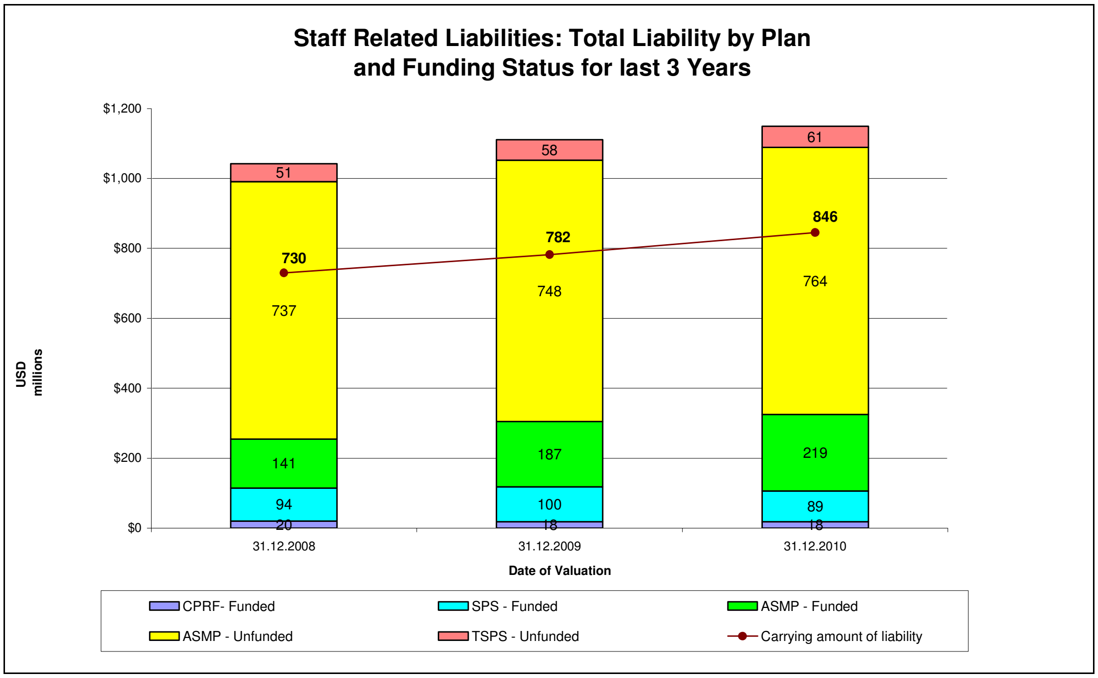
Plan	**2010**	*% of total liability*	**2009**	*% of total liability*	**2008**	*% of total liability*
CPRF	17.6	*1.5%*	18.0	*1.6%*	20.5	*2.0%*
TPF	22.9	*2.0%*	21.1	*1.9%*	20.4	*2.0%*
SPS	88.5	*7.7%*	89.6	*8.1%*	92.5	*8.9%*
ASMC	714.6	*62.1%*	653.7	*58.8%*	596.5	*57.2%*
Total accrued liabilities	**843.6**	*73.4%*	**782.4**	*70.4%*	**729.9**	*70.0%*
Add: Unrecorded liabilities	306.3	*26.6%*	328.4	*29.6%*	312.3	*30.0%*
Total actuarially determined liabilities	**1,149.9**	*100.0%*	**1,110.8**	*100.0%*	**1,042.2**	*100.0%*
Less: Earmarked long-term investments (at Fair Market Value)	(316.3)	*27.5%*	(294.8)	*26.5%*	(242.3)	*23.2%*
Less: Advances to staff on SPS	(8.7)	*0.8%*	(10.1)	*0.9%*	(12.5)	*1.2%*
Total unfunded liabilities *	**824.9**	*71.7%*	**805.9**	*72.6%*	**787.4**	*75.6%*
* Of which:						
TPF	60.8		58.2		50.6	
ASMC	764.1		747.7		736.8	
Total unfunded liabilities	**824.9**		**805.9**		**787.4**	

[2] Recorded liabilities totaled USD 843.6 million at 31 December 2010. Unrecorded liabilities of USD 306.3 million reflect the use of the corridor method for recognising actuarial gains and losses, in accordance with International Public Sector Accounting Standards (refer to para. 7 for discussion of corridor method).

[3] Unfunded liabilities totaled USD 824.9 million at 31 December 2010.

[4] Earmarked long-term assets include outstanding advances to staff members on final Terminal Emoluments.

Graph 1



7. As shown in Table 3, the Organization has deferred recognition of USD 306.3 million of the actuarially determined liability as at 31 December 2010. In line with current International Public Sector Accounting Standards (IPSAS) guidance, the Organization has adopted the policy of utilizing the corridor method to recognize actuarial gains and losses. Under this method, actuarial gains and losses that exceed 10 per cent of the value of the actuarial liability are deferred and recognized over the expected average remaining working lives of the employees participating in the plan, which is currently estimated from 9.4 to 11.4 years. FAO opted for this method over immediate full recognition as it mitigates significant volatility in the reported value of the Plan liabilities caused by external factors, such as movements in the EUR-USD exchange rate and discount rates, which are entirely out of FAO's control and which may ultimately offset over time. Of the total amount deferred, USD 268.1 million (2009 – USD 280.8 million) relates to ASMC; USD 37.9 million (2009 – USD 37.1 million) relates to TPF; and USD 0.3 million (2009 – USD 10.5 million) relates to SPS.

8. It should be noted that in the future the IPSAS guidance could change with respect to the corridor method and instead recommend the immediate recognition of all actuarial gains/losses.

9. During 2010, the carrying value of long-term investments earmarked by the Organization for the Plans increased by USD 21.5 million from USD 294.8 million at 31 December 2009 to USD 316.3 million at 31 December 2010. For comments on investments reference should be made to document FC 138/INF/2.

Accounting and Funding

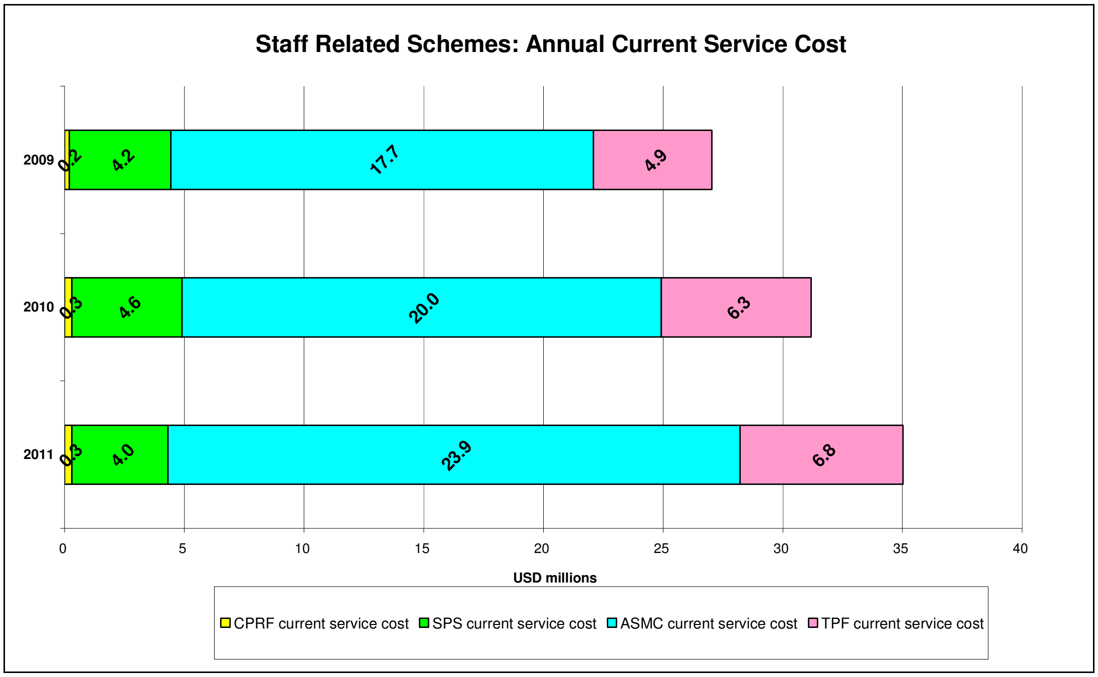
10. Table 4 and Graph 2 below show the annual Current Service Costs[5] for the three years ending 31 December 2011, which are based on the actuarial valuations for the preceding years at 31 December 2010, 2009 and 2008, respectively.

Table 4

(in USD Millions)

Plan	2011	% total expense	2010	% total expense	2009	% total expense
CPRF	0.3	*0.9%*	0.3	*1.0%*	0.2	*0.7%*
TPF	6.8	*19.4%*	6.3	*20.2%*	4.9	*18.1%*
SPS	4.0	*11.4%*	4.6	*14.7%*	4.2	*15.6%*
ASMC	23.9	*68.3%*	20.0	*64.1%*	17.7	*65.6%*
Total	**35.0**	***100.0%***	**31.2**	***100.0%***	**27.0**	***100.0%***

Graph 2



[5] The current service cost is a standard component of staff costs and arises each year as active staff members provide their services in exchange for these benefits to be paid in the future. Reported amounts represent total current service cost for staff members working on both Regular Programme (RP) and Extra-budgetary (EB) activities. In 1997 the Governing Bodies recognized that current service cost related to RP staff members be funded each biennium from the Regular Programme Budgetary appropriation and expensed in the official accounts among costs to deliver the current programme of work of FAO. Current service cost for EB staff members is charged to trust fund project expense and, therefore, funded through project revenues. Funding of actuarial losses (i.e. increases in the liability as a result of adverse experience as compared to actuarial estimates) is considered in the overall funding requirements for past service liabilities.

The increase in the total current service cost is mainly due to the rise in that of the ASMC. This is due to:

- increases due to the change in the discount rate from 5.4% to 5.0% for USD 2.7 million
- increases due to the change in the participation and spousal coverage at retirement of USD 2.0 million

offset by decreases for the movement in the EUR-USD exchange rate of USD 1.2 million.

11. Conference Resolutions 10/99 and 10/2001 provide that long-term investments and any income which they generate are to be applied first to ensure the adequacy of funding of the SPS and CPRF. The Resolutions also provided that any additional investments and related income then be earmarked for the ASMC and subsequently for the TPF. As of 31 December 2010, both the ASMC and TPF continue to be underfunded (refer also to Table 3 and Graph 1). The earmarking of the long-term investments and the SPS advances to the plans is shown in Table 5 below.

Table 5

(in USD Millions) **Plan**	**2010**	**2009**	**2008**
Fully funded			
CPRF	17.6	18.0	20.5
SPS	88.8	100.1	93.5
Partially funded			
ASMC	218.6	186.8	140.8
Unfunded			
TPF	0.0	0.0	0.0
Total funded liabilities	**325.0**	**304.9**	**254.8**
Funded by:			
Earmarked long-term investment	316.3	294.8	242.3
Advances to staff on SPS	8.7	10.1	12.5
	325.0	**304.9**	**254.8**

12. In accordance with Finance Committee and FAO Council guidance, the Secretariat has obtained from FAO's actuaries the annual amounts required to fully fund the ASMC and TPF liabilities using target dates of 31 December 2040 and 31 December 2025, respectively.

13. Based on the most recent actuarial valuation as of 31 December 2010, in order to fully fund the TPF past service liability of USD 60.8 million (using a 15-year amortization period starting in 2010), the Organization would need to contribute an additional USD 5.3 million per year (USD 10.6 million per biennium).

14. Based on the most recent actuarial valuation as of 31 December 2010, in order to fully fund the US Dollar value of the ASMC past service liability of USD 764.0 million (using a 30-year amortization period beginning in 2010), USD 25.5 million per year (USD 51 million per biennium) would need to be contributed. By comparison, assessments on Member Nations towards funding of the past service ASMC liability for the biennium 2010-11 currently amount to USD 7.05 million per year (USD 14.1 million per biennium) as approved by Conference in November 2009. This level of funding, based on the original target funding date of 31 December 2027, was first approved by Conference in November 2003 for the 2004-05 biennium, and has

remained unchanged through subsequent biennia, notwithstanding the increase in the unfunded amount of the ASMC.

Comparison with other UN Organizations

15. As previously reported in FC 132/3 *2009 Actuarial Valuation of Staff Related Liabilities*, the United Nations Secretary General is to submit a report on managing the UN's ASMC liabilities to the 67th session of the General Assembly. The 67th session has not yet been held (due 2012). It should be noted that UN-wide ASMC information is provided for comparison purposes only and that the responsibility of addressing the funding of the liabilities lies with the Governing Bodies of each individual organization. This was also emphasized in the report of the Joint Inspection Unit (JIU/REP/2007/2) where it was recommended that the "*legislative bodies of each organization should provide adequate financing to meet the liabilities*".

16. For information purposes, Table 6 below shows a comparison of the ASMC liability of UN system organizations at 31 December 2009, 2008 and 2007.

Table 6

Comparative analysis of ASMC liability for UN system organizations

Organization	Total Liability (USD million)			Funding Available (USD million)			Liability recorded on the Balance Sheet (USD million)			Liability not yet recorded on the Balance Sheet (USD million)		
	31-Dec-07	31-Dec-08	31-Dec-09	31-Dec-07	31-Dec-08	31-Dec-09	31-Dec-07	31-Dec-08	31-Dec-09	31-Dec-07	31-Dec-08	31-Dec-09
FAO	576.1	878.0	934.5	200.7	141.0	186.7	576.1	596.0	653.6	-	282.0 (a)	280.9 (a)
IAEA	207.0	225.0	244.0	-	-	-	-	-	-	207.0	225.0	244.0
ICAO	55.2	46.8	54.2	-	-	-	-	-	-	55.2	46.8	54.2
IFAD	41.0	50.0	61.3	46.0	57.0	60.0	41.0	50.0	61.3	-	-	-
ILO	415.0	499.4	509.5	-	27.9	36.2	-	-	509.5	415.0		-
IMO	22.1	22.7	N/A	-	-	N/A	-	-	N/A	-	-	N/A
ITC	50.8	53.8	37.1	-	-	-	50.8	53.8	37.1	-	-	-
ITU	181.3		188.0	-		-	-	-	-	181.3		188.0
PAHO	-	167.0	202.6	-	18.3	22.3	-	-	-	-	148.8	180.3
UN	2,433.0	2,596.0	2,302.5	-	-	-	2,431.0	2,596.0	2,302.5	-	-	-
UNDP			N/A			N/A			N/A			N/A
UNESCO	614.0		649.0	30.0		27.2	-	-	-	614.0		649.0
UNFPA	72.8	72.8	87.5	61.2	70.0	79.0	72.8	72.8	87.5	-	-	-
UNHCR	308.0	307.8	347.4	-	-	-	308.0	307.8	347.4	-	-	-
UNICEF	292.0	483.0	464.0	150.0	180.0	210.0	-	-	-	292.0	483.0	464.0
UNIDO	104.9	104.9	100.5	-	-	-	-	-	-	104.9	104.9	100.5
UNRWA			N/A			N/A			N/A			N/A
UNWTO	3.2	3.2	3.8	-	-	-	-	-	-	3.2	3.2	3.8
UPU	5.6	5.6	5.6	-	-	-	-	-	-	5.6	5.6	5.6
WFP	150.5	165.2	181.8	87.5	93.5	107.4	150.5	165.2	181.8	-	-	-
WHO	383.6 (b)		1,000.0 (b)	384.0		450.0	341.0		450.0	42.6		550.0
WIPO	74.1	73.9	98.9	-	-	-	33.8	36.8	45.5	40.4	37.1	53.4
WMO	75.0	75.0	59.5	1.0	1.3	1.7	-	-	-	75.0	75.0	59.5

N/A - Information not currently available
(a) Liability not yet recorded on the Balance Sheet reflects FAO's use of the corridor method, as permitted under IPSAS 25, for deferring recognition of a portion of actuarial liabilities.
(b) - 2007 liability restated (USD 649m to USD 384m) due mostly to non-consolidation of entities. 2009 liability is an estimate based on a 2008 actuarial study and will be updated.