JIU/NOTE/91/2

NOTE ON CONTINGENCY MARGIN OF UNITED NATIONS INDUSTRIAL DEVELOPMENT ORGANIZATION BUDGET

Prepared by
Siegfried Schumm

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I. INTRODUCTION

1. The Joint Inspection Unit issued a report on budgeting of organizations of the United Nations System (JIU/REP/89/9 Vols. I and II), in which the Inspector has indicated his intention to conduct follow-up studies on specific issues. The Inspector became aware of the increasing problems of UNIDO's budgeting and financing in connection with its contingency margin, which has complicated the serious financial situation at UNIDO by creating administrative and management difficulties. The JIU has decided to present a Note specifically on the contingency margin of UNIDO, which was introduced in 1988-1989 as a 15 per cent "reserve of appropriations".

2. When issuing the above-mentioned JIU report, the Inspector had some hesitation in recommending the establishment of a contingency margin 1/. The following recommendation of the report reflected some caution:

> Recommendation 4: Organizations should closely review the experience gained by other organizations which have applied a "contingency margin", and consider the possibility of its introduction, after having discusssed such a possibility with CCAQ(FB) 2/.

3. Subsequently, the Consultative Committee on Administrative Questions (Financial and Budgetary Questions) (CCAQ(FB)) discussed this matter in some detail and in this respect it is important to quote Administrative Committee on Co-ordination (ACC) comments 3/.

> "10. After discussion in CCAQ as recommended, ACC has found no evidence that contingency margins encourage prompt payment of assessed contributions. Indeed, the available experience suggests that the opposite is the case, and that the most likely effect of contingency margins would be to lead Member States to limit their payments on the assumption that the programme and the budget were not authorized for full implementation. This would introduce an element of uncertainty about the programme to be implemented, or make the implementation of the programme dependent on the timing of payment of contributions.

1/ JIU/REP/89/9 Vol. I, paras. 51 and 52.

2/ Ibid, p.31.

3/ ACC/1990/5, Recommendation 4, paragraphs 10-11, pp. 33-34.

"11. It is, however, the question of principle which arises in this connection that constitutes, in the view of ACC, the most serious objection to contingency margins in the budgets of organizations of the system. The existence of such margins would imply that Member States had the option of not honouring the obligations provided for in the constitutional instruments and financial regulations to which they had subscribed in joining the organizations. ACC believes that there can be no compromise with the principle that when governing bodies approve a programme and a budget they intend them to be carried out in full. Member States then have an obligation to pay in full and on time the contributions required for this purpose."

4. The Inspector believes the time has now come to review and reconsider the application of the contingency margin in the light of the experience of UNIDO over the biennia 1988-1989 and 1990-1991. The experience of UNIDO in this regard will be of considerable interest to other organizations of the United Nations system.

II. EXECUTIVE SUMMARY

5. After conducting a review of the application of the contingency margin and its impact on UNIDO's activities and in the light of ACC comments, the Inspector concludes that:

(i) the introduction of a contingency margin does not assist in the financial management of the funds available to the Organization, disrupts the smooth planning of programme implementation and causes serious administrative difficulties;

(ii) the imposition of a mandatory contingency margin goes against the principle that approved programme and budgets should be carried out in full;

(iii) a contingency margin does not encourage Member States to pay their assessed contributions in full and on time.

III. RECOMMENDATION

6. The Inspector recommends that UNIDO discontinue the practice of introducing mandatory contingency margins through "reserves of appropriations" for its programme and budgets from the 1992-1993 biennium onwards.

IV. CONTINGENCY MARGINS

7. It should be recalled that the contingency margin as considered by JIU was expected to achieve the following objectives:

(a) to encourage the Organization to set priorities in executing programmes, thereby leading to a higher degree of efficiency;

(b) to encourage Member States to pay their contributions on time;

(c) to improve the cash management procedures of the Organization.

8. In the opinion of the Inspector, the original purpose and intent of the contingency margin may not have been clearly understood. In particular:

(a) a contingency margin is not a reserve of funds (the term "reserve" appears misleading since a reserve normally represents the setting aside of funds);

(b) a contingency margin should not lead to a reduction in the approved level of an authorized budget;

(c) a contingency margin is not an appropriate means to alleviate financial difficulties pending the receipt of assessed contributions;

(d) Member States should not use the presence of a contingency margin as grounds to delay their consitutional obligations, i.e. to pay the assessed contributions on time.

V. APPLICATION OF THE CONTINGENCY MARGIN AT UNIDO

9. A contingency margin was established according to the resolution adopted in 1987 by the General Conference of UNIDO. It applied to its programme and budget for the 1988-1989 biennium and was re-applied for 1990-1991. From the total amount of the appropriations of these bienniums, it was decided "to keep in reserve" an amount representing 15 per cent of those appropriations "pending receipt from Member States of their assessed contributions" (decisions GC.2/Dec.22 and GC.3/Dec.23).

10. UNIDO's resolution implied that only 85 per cent of the programme activities could be obligated, and that only when sufficient contributions had been received could the remaining activities be obligated. The percentage for the contingency margin was determined primarily on the basis of the then expected collection rates of assessed contributions.

11. Experience has shown that the introduction of the contingency margin did not achieve the original objective of such margins. Instead, it exacerbated an already difficult situation, stemming from the non-payment or delayed payment of the assessed contributions by the Member States. If Member States fulfilled their legal obligations, a series of complicated and costly administrative tools in place to alleviate the situation would not be necessary.

12. The financial problems of UNIDO, which were in evidence before the introduction of the contingency margin, have not improved as a result of the introduction of the margin. In fact, the delayed payments of assessed contributions continue to disrupt the planning and programme execution of the programme budget for which Member States took the responsibility and entrusted the Director-General to fully implement.

Difficulty in planning and programme implementation

13. The contingency margin of UNIDO does not allow for smooth planning of activities by the Organization in line with the approved budgets. The 15 per cent contingency margin has resulted in partial implementation of programmes on the basis of "cash budget", whereby activities are often commenced or postponed subject to receipt of assessed contributions. This results in "stop/go" budgetary implementation.

14. In applying the contingency margin, UNIDO faces additional administrative difficulties given the structure of UNIDO's budget and the nature of some of the programmes. For example:

(a) on-going staff costs represent a large proportion of the budget (approximately 76 per cent of the regular budget) and the Organization has difficulty in recruiting highly qualified staff for short-term periods;

(b) some activities in UNIDO cannot operate on a reduced appropriation level (e.g. the Secretariat of the Policy-making organs, the Regular Programme of Technical Assistance and the Industrial Development Decade for Africa Programme);

(c) under common services arrangements for the Vienna International Centre (VIC) - as set out in the Memorandum of Understanding - UNIDO has clear-cut responsibilities to other UN organizations. For example, UNIDO is responsible for providing services (buildings management, etc.) and to assume its cost sharing of services provided by the other organizations (security, printing, library, medical, etc.). The contingency margin of 15 per cent of the appropriations is disruptive and leads to poor working relationships with other organizations, which expect a certain level of service to be provided by UNIDO and full payment for agreed cost-sharing arrangements. The full costs of the services and reimbursements are included in the approved programme budget.

In consequence: Since the contingency margin cannot be applied to some of UNIDO's programme budget activities, to achieve a 15 per cent margin would require a larger margin for the substantive activities, which should be the raison d'etre of the Organization.

15. UNIDO has an almost unmanageable task to operate within available cash resources, especially since the Organization has no authority to borrow funds. In the circumstances, the requirement for a contingency margin restricts UNIDO's ability to manage its financial resources. UNIDO's financial management should take into account the following considerations:

(i) anticipated assessed contribution receipts based on previous experience or information received from Member States;

(ii) level of unliquidated obligations which can be paid for from late paid contributions;

(iii) other regular budget cash resources available to the Organization (e.g. Working Capital Fund, budgetary surpluses);

(iv) other organizational liabilities (i.e. United Nations loan);

(v) cash-flow requirements for the future financial year;

(vi) replenishment of the Working Capital Fund from previous years' unutilized economies;

(vii) inability to borrow funds.

VI. CONCLUDING COMMENTS

16. In the view of the Inspector, the contingency margin pending the receipt of assessed contributions is in conflict with the Organization's responsibility to fully implement the programme and budget approved by the Member States. It is simply not logical that Member States, while not fulfilling their legal obligations to provide the Organization with necessary resources, hamper the Secretariat in implementing the approved programme budget.

17. It should not be under-estimated that some Member States may have further delayed their payments on the misunderstanding that the contingency margin is "a reserve". Experience has shown that, during the budgetary periods concerned, an increasing number of Member States tended to pay their assessed contributions late with some delaying payment until towards the end of each year. The Inspector is seriously concerned that this contingency margin has been used, in some cases, as a pretext not to pay, or to delay the assessed contributions.

18. The Inspector sees no objective reasons why such a margin should be formalized to the detriment of the necessary flexibility of UNIDO management in implementing the approved programme budget. If necessary resources are not available, the Director-General has, in any event, to adjust the implementation of the approved programme budget to remain within available resources. This would lead to more efficient financial management than can be achieved by imposing a contingency margin which only serves to straitjacket the Organization.

19. This contingency margin has resulted in delayed implementation or cancellation of activities, since the 15 per cent "withholding reserve" prevents the timely obligation of programme activities. This leads inevitably to larger budgetary surpluses, which could not have been the intention of Member States in approving the budget resolution which calls for full implementation of the programme budget.

20. The failure by Member States to meet their financial obligation to international organizations is a serious and an ongoing problem within the United Nations system. The introduction of mandatory restrictions on the use of appropriations through contingency margins or withholding of appropriations increases the difficulties of the United Nations organizations in managing financial resources and implementing programmes in a planned and efficient manner.