



**FORTY-FIFTH MEETING OF THE
COMMITTEE OF REPRESENTATIVES OF GOVERNMENTS AND ADMINISTRATIONS**
(Alofi, Niue, 31 October – 2 November 2015)

AGENDA ITEM 9.3: 2015 REVISED BUDGET AND 2016 PROPOSED BUDGET

(Paper presented by the secretariat)

Summary

1. This paper presents the Pacific Community's (SPC) proposed budget for financial year 2016 for consideration and approval by CRGA.
2. It also presents the revised 2015 budget to CRGA for noting, in accordance with SPC's Financial Regulations, which require the Director-General to inform CRGA of revisions of the budget.
3. The revised 2015 budget is a balanced budget, totalling 113.978 million CFP units, comprising the core budget of 26.57 million CFP units and programme and project funding of 86.796 million CFP units in income and expenditure. A contribution of 605,000 CFP units was made to balance the revised 2015 budget, based on the CRGA 43 authorisation to use 688,000 for that purpose. Overall, the 2015 revised budget reflects a small increase of 3.027 million CFP units, or around 2.7% compared to the original budget of 110.951 million CFP units.
4. The secretariat proposes a balanced 2016 budget of 93.39 million CFP units, comprising the core budget of 26.986 million CFP units and programme and project funding of 66.404 million CFP units. This is a significant decrease from previous years due in the main to a gap between the end of cycles of project funding and the start of new cycles (e.g. European Development Fund – EDF11). This context also has an impact on the budget projections for 2017 and 2018 as outlined below.
5. This paper also draws CRGA's attention to a projected deficit of 2.597 million CFP units in 2017 and 3.818 million CFP units in 2018.
6. Notwithstanding the tight financial situation, in order to balance the 2016 budget the secretariat was able to cover a deficit of 1.2 million CFP units, to which members' attention was drawn at CRGA 44. This was done by means of internal cost savings across technical divisions and operations and management. Even in this difficult context, the secretariat has been able to contribute funding to strengthen SPC's reserves in the 2016 budget, as a means of responding to previous requests from CRGA to address the level of reserves, and as a matter of corporate responsibility.

7. The secretariat is committed to addressing the projected budget deficits and to raising the resources necessary to fund initiatives under the Pacific Community Strategic Plan 2016–2020, together with any new or emerging priorities. The recruitment of a new Director of Finance and the implementation of sustainable financing initiatives over the next three budget cycles are part of the secretariat's strategy to ensure that SPC's financial systems and levels of funding are truly fit for purpose and placed at the service of the priorities on which the organisation will focus.

Recommendations

8. CRGA is invited to:
 - i. note the revised 2015 budget;
 - ii. approve the proposed budget for financial year 2016;
 - iii. approve the secretariat's request to use 600,000 CFP units from reserves to fund priorities and initiatives under the new Pacific Community Strategic Plan in 2016;
 - iv. recognise the serious budgetary situation for 2017 and 2018;
 - v. acknowledge the positive efforts made by the secretariat to strengthen SPC's reserves;
 - vi. approve the secretariat's plans to further develop and implement a sustainable financing strategy, including cost recovery and priority setting mechanisms, over the next three budget cycles.
-

2015 REVISED BUDGET AND 2016 PROPOSED BUDGET

Purpose

9. This paper presents SPC's proposed budget for financial year 2016 for consideration and endorsement by CRGA. It also presents the revised 2015 budget to CRGA for noting, in accordance with SPC's Financial Regulations, which require the Director-General to inform CRGA of revisions of the budget.

Introduction

10. The proposed 2016 budget and the revisions to the 2015 budget are contained in the 'green budget book'. It includes the income budget and expenditure budget, and also a summary of expenditure by budget chapter (i.e. by division).

Revised budget for 2015

11. The revised 2015 budget is a balanced budget totalling 113.978 million CFP units, comprising the core budget of 26.57 million CFP units and programme and project funding of 86.796 million CFP units in income and expenditure. Overall, the 2015 revised budget reflects a small increase of 3.027 million CFP units or around 2.7% compared to the original budget of 110.951 million CFP units. The secretariat draws CRGA's attention to the fact that although CRGA 44 approved a balanced budget, in reality – due to currency fluctuations – the secretariat has had to deal with a budget deficit from the outset in 2015. This has hindered the ability to reallocate resources to new and emerging priority areas over 2015 as any savings or reductions in expenditure were used to redress this situation. Moreover, to finally balance the revised 2015 budget, it was necessary to inject 605,000 CFP units from the reserves, on the basis of CRGA 43's authorisation of the use of a total of 688,000 CFP units for this purpose. The remaining 83,000 CFP units have been returned to the reserves in the 2016 budget.

Proposed budget for 2016

12. The secretariat proposes a balanced 2016 budget of 93.39 million CFP units, comprising the core budget of 26.986 million CFP units (around 28.9% of the total budget) and programme and project funding of 66.404 million CFP units. This is a significant decrease from previous years due in the main to a gap between the end of cycles of project funding and the start of new cycles (e.g. EDF11).
13. In line with SPC's long-standing policy, only assured funding is included in the budget; prospective funding from pipeline projects is not included.
14. The secretariat is committed to addressing the projected budget deficits and to raising the resources necessary to fund initiatives under the Pacific Community Strategic Plan 2016–2020, together with any new or emerging priorities. To achieve this, the secretariat has recruited its first dedicated Director of Finance, Mr Martin Van Weerdenburg, and intends to place a more strategic focus on its finances. Cost recovery will be implemented across the organisation beginning in 2016, with the objective of full implementation by the end of three budget cycles. A dedicated resource mobilisation function will also be created.

15. The need to ensure sustainable financing for SPC in the future will most certainly require the secretariat and members to revise their approach to work programmes and investment. Core and surplus funding must in future be allocated according to an objective priority setting mechanism, so that SPC's finances can be placed at the service of the organisation's strategic objectives rather than simply distributed on a historical basis. The ultimate objective is to have a sustainable financing strategy in place and fully implemented by the end of FY 2018, so that the organisation's financial systems and funding levels are truly 'fit for purpose'.

Terms used in the paper

16. Funding in the 2015 revised budget and proposed 2016 budget is classified under the headings of *core funding*, *programme funding* and *project funding*:
 - i. *Core funding* is wholly unrestricted in its use and refers to income received from the following sources: members' assessed contributions, host country grants, and general income (such as management fees, bank interest, miscellaneous income, and service fees charged by the Educational Quality and Assessment Programme – EQAP). It also includes contributions from members (e.g. Australia, France and New Caledonia) to fund the secretariat's core business operations. Core funding is generally not time bound and therefore provides a predictable source of income for the organisation in the future.
 - ii. *Programme funding* refers to income received from members and donors for use in a broad thematic area or by a specific division, but not tagged to a specific project. There is thus a degree of flexibility in deploying programme funds within the selected area of focus. Such funding is generally time-bound.
 - iii. *Project funding* refers to contributions by development partners, including both SPC members and non-members, that are earmarked for specific time-limited activities.

Structure of the budget

17. Supporting the income and expenditure budget summary on pages 1 to 4 of the green budget book is each division's budget by budget chapter, which shows:
 - funding categories – core and project funding;
 - budget narratives, which describe for each division/programme its goal, objectives and key planned outputs/results to be achieved under core and project funding for FY 2016; and
 - an early budget prediction for the next two years, FY 2017 and FY 2018, alongside the FY 2016 budget and FY 2015 revised budget.
18. The green budget book also contains a number of annexes with supporting information, such as 2016 assessed contributions and host grants, and an early income prediction to 2018 by funding type and by source (member/donor), and allocation of core funding.

Budget assumptions

19. Assessed contributions for the FY 2015 revised budget, and FY 2016 and FY 2017–2018 are at levels agreed to at the 8th Conference of the Pacific Community. In FY 2016 the metropolitan members contribute 9,167,665 CFP units made up of:

| | |
|-------------|----------------------------|
| Australia | 3,200,000 CFP units |
| France | 2,500,000 CFP units |
| New Zealand | 2,050,000 CFP units |
| <u>USA</u> | <u>1,417,665 CFP units</u> |
| Total | 9,167,665 CFP units |

20. The 22 island members of SPC contribute a total of 2,113,600 CFP units in assessed contributions. Each such member falls within one of the five categories of membership contributions, as endorsed by the 8th Conference. Individual members' contributions are shown in Annex 1 of the green budget book.
21. The 8th Conference also noted the request from Guam to review its capacity to pay an increased assessed contribution of 130,000 CFP units per annum, under category 2, after 2015. Guam's contribution in the budget is therefore still at the 2014 amount (69,000 CFP units), pending information on its capacity and willingness to pay this new level of assessed contribution. The secretariat would welcome a formal communication from Guam on this matter.
22. As regards host country grants, it should be noted that the 8th Conference acknowledged the proposal to increase the total amount of host grants to 3,000,000 CFP units by fiscal years 2015/2016. Given the financial situation of SPC's host countries and the global economic context, the secretariat considers that that amount is unrealistic. It has, therefore, proposed a more modest increase and this is the basis on which consultations have taken place over 2015. If host countries do indeed make the level of contribution requested, the new amount of host country grants would be as follows:

| Host country | New proposed amount | 2016 amount | 2015 amount |
|-----------------|---------------------|--------------------|-------------------|
| Fiji | 400,000 CFP units | 40,000 CFP units* | 40,000 CFP units |
| New Caledonia | 340,000 CFP units* | 340,000 CFP units* | 60,000 CFP units |
| FSM | 200,000 CFP units | 0 | 0 |
| Solomon Islands | 50,000 CFP units* | 50,000 CFP units* | 50,000 CFP units |
| TOTAL | 990,000 CFP units | 430,000 CFP units | 150,000 CFP units |

* These amounts have already been agreed to by the host countries.

23. For FY 2016, host country grants have been increased from their previous total level of 150,000 CFP units to 430,000 CFP units. This increase is the result of positive discussions with the Government of New Caledonia which committed to a significant increase in its host grant from 60,000 CFP units to 340,000 CFP units per annum. The Secretariat acknowledges this effort with much appreciation.
24. Discussions are still underway with Fiji to increase its host country contribution from the current annual level of 40,000 CFP units to 400,000 CFP units. Fiji is currently undertaking internal consultations, which the secretariat hopes will allow it to meet this target from 2016 onward, and has been in regular contact with the secretariat on this matter. The 8th Conference approved the introduction of an annual host grant of 50,000 CFP units for Solomon Islands, which has been paid since 2014 and is included in the 2016 budget figures.

25. Federated States of Micronesia, which has hosted SPC's North Pacific Regional Office since January 2006, remains the only SPC host country that does not currently make a host country contribution to the organisation. At the date of writing, FSM has not confirmed its capacity to pay a contribution of 200,000 CFP units per annum. However, the secretariat has been informed that this will be proposed to the FSM congress before year's end. Any further information in this regard from FSM would be greatly appreciated.
26. In this context, the FY 2016 budget only reflects the host country grant amounts that have been formally agreed to. The secretariat intends to pursue discussions with Fiji and FSM. If the outcome of these discussions is positive, this would provide a significant contribution to strengthening SPC's core funding, in particular over the period of the new Pacific Community Strategic Plan.
27. General income (such as project management fees, bank interest) is forecast taking into account 2015 income to date, current market rates and approved projects.
28. Programme funding that is tagged or designated for the delivery of specific divisional outputs is shown separately from programme funding that is available for use as determined by SPC. Designated programme funding is received from Australia (EDD,¹ FAME, PHD) New Zealand (GSD, FAME, LRD, PHD, SDD, SPL) and New Caledonia (FAME, Maintenance Grant).

REVISED 2015 BUDGET OVERVIEW

29. The revised 2015 budget is a balanced budget totalling 113.978 million CFP units, comprising the core budget of 26.57 million CFP units and programme and project funding of 86.796 million CFP units in income and expenditure. Overall, the 2015 revised budget reflects a small increase of 3.027 million CFP units or around 2.7% compared to the original budget of 110.951 million CFP units. As mentioned above, the revised budget was balanced through a contribution of 600,000 CFP units from reserves based on a previous CRGA authorisation.

Core funded budget 2015

30. Core income – the main increase of 307,600 CFP units is a result of an increase in management fees over the course of FY 2015.

Project funded budget 2015

31. Projects total 77.851 million CFP units in the revised 2015 budget, which is a decrease of 129,400 CFP units from the original budget of 77.981 million CFP units. The decrease is due primarily to the closure of the Grants Management Unit following SPC's withdrawal from principal recipient status with the Global Fund.

¹ Abbreviations for SPC technical divisions used in this paper: GSD – Geoscience Division; EDD – Economic Development Division; EQAP – Educational Quality and Assessment Programme; FAME – Fisheries, Aquaculture and Marine Ecosystems Division; LRD – Land Resources Division; PHD – Public Health Division; SDD – Statistics for Development Division; SOC – Social Development Division; OMD – Operations and Management Directorate; SPL – Strategy, Programming and Learning Unit.

PROPOSED 2016 BUDGET OVERVIEW

32. A balanced 2016 budget of 93.39 million CFP units is proposed to CRGA, comprising the core budget of 26.986 million CFP units, and programme and project funding of 66.404 million CFP units. The core budget makes up around 28.9% of the total budget.
33. Members contribute 44% of the total budget (metropolitan members 41.2%, Pacific Island members 2.8%). Development partners contribute 47.4%, and the remaining 8.6% comes from other internal income sources.
34. The green budget book presents a summary of income by type (core, programme and project funding).
35. Chapter I – Director-General's Office and Deputy Directors-General – covers the budget of the Director-General's office and the offices of the two Deputy Directors-General.² It also includes the Strategy, Programming and Learning Unit, Communications and Public Information and the new Climate Change and Environmental Sustainability Programme, to which France has contributed significant funding following the High Level Dialogue with President François Hollande convened by SPC in November 2014. Together, these units account for 13.2% of the total budget.
36. Chapters II–IX cover the budgets of all the technical divisions under the Programme Directorate. The Geoscience Division continues to be the largest of the seven technical divisions with 19.7% of the total SPC budget. The Land Resources Division and Economic Development Division account for 13.1% and 13% respectively of total SPC funding. The Fisheries, Aquaculture and Marine Environment (FAME) Division accounts for 11.1% of the budget; Statistics for Development, 4.7%; Public Health Division, 3.7 %; Social Development Division, 3.3%; and Educational Quality and Assessment Programme (formerly SPBEA), 2.2%.
37. Chapter X deals with the Operations and Management Directorate (OMD), which provides support for the work of the organisation across eight broad areas: administration, finance, human resources, ICT, legal services, library services, publications and printery, translation and interpretation. OMD also includes SPC's decentralised offices (North Pacific Regional Office and Solomon Islands Country Office) and houses the PIRMCCM³ secretariat. OMD represents 11.3% of the total budget.
38. Chapter XI – Common charges cover overhead costs such as maintenance and operating costs of facilities, utilities, telecommunication, general insurance and the governing council. Common charges form 2.2% of the total budget.
39. Chapter XII – The Housing Unit and canteen are both self-funded operations. Any surpluses or deficits are transferred to the special funds reserve at the end of each financial year.

² From 2016 onward, the position of Deputy Director-General (Programmes) will no longer exist and the secretariat will revert to a structure with two DDGs (one based at HQ in Noumea and the other in the Suva Regional Office) who will share executive support and leadership functions in support of the Director-General.

³ Pacific Islands Regional Multi-Country Coordinating Mechanism.

Core-funded budget 2016

40. The core-funded budget is balanced mainly due to a series of internal cost saving measures taken by the secretariat that have allowed the organisation to absorb the projected 2016 deficit of 1.126 million CFP units. OMD has contributed around 500,000 CFP units to this effort, mainly through freezing vacant positions (which would otherwise have been used to ensure strengthening and continuity of OMD functions), and all divisions voluntarily accepted a reduction of at least 50,000 CFP units in their 2016 core allocation. Moreover, after a robust discussion by the Senior Leadership Team (SLT), it was decided to reduce the core funded travel budget by 25% across the organisation in 2016 and to put a moratorium on all core funded meetings in 2016 except for CRGA itself. SLT also decided to freeze recruitment of any new positions on core funding for 2016, except if such positions are deemed critical for reasons of service. The secretariat draws members' attention to the efforts that have been made to control costs and expenditure while at the same time attempting to maintain the level and quality of staffing and resourcing necessary for SPC to avoid a major reduction in its services to the region.
41. Whilst the budget is balanced for FY 2016, as of writing and on the basis of current levels of funding and activity, the organisation may face a deficit of 2.597 million CFP units in 2017 and 3.818 million CFP units in 2018. As new projects and programmes come online, and as the secretariat implements more consistent cost recovery mechanisms for all such new projects, it is expected that these deficits will be reduced.
42. The fall in the AUD since 2013 continues to adversely affect core income. As in 2014, this decline may negatively affect the 2016 core budget by decreasing core income. As a precaution, in 2015 the secretariat hedged AUD currency at 80 points. For 2016, however, the rate has already fallen below 75 points. Should that situation continue, there may be a negative impact of around 800,000 CFP units on the 2016 core budget.
43. The 2016 income situation is also affected by uncertainty surrounding the possibility of Fiji increasing its host country grant and FSM paying a host country grant. Apart from New Caledonia's commitment to a higher host country contribution and in the absence of a confirmation from Fiji and FSM, no additional levels of host country contribution have been included as income in the 2016 budget.
44. The secretariat draws members' attention to the fact that, under current financial circumstances, once all core-funded allocations have been made in order to allow SPC to carry out its missions in 2016, management has very little leeway to fund any new priorities including those identified under the new Pacific Community Strategic Plan. It will, therefore be necessary to undertake a robust priority setting exercise so that SPC's resources are aligned with its priorities and will contribute to development effectiveness in those areas.
45. However, at year's end, SPC will transfer 1.3 million CFP units to reserves (from general provisions and operating surplus), under the requirements of the International Public Sector Accounting Standards (IPSAS), which indicate that the secretariat can no longer roll these funds over to the new financial year without an authorisation to do so from the governing body.

46. In light of the information contained in the previous paragraph, and of the need to create a pool of disposable core funds to begin addressing new priorities under the Strategic Plan, the secretariat requests CRGA's approval to withdraw 600,000 CFP units from the 1.3 million CFP units that will be contributed to reserves in the 2016 budget. This would provide a disposable pool of funding for new priorities in 2016 and still allow the organisation to strengthen its reserves by 700,000 CFP units. The secretariat also draws members' attention to the discussion on reserves in paragraphs 53–56, which show that SPC will reach the 2015 target of increasing its reserves to over 5 million CFP units, notwithstanding the use of 600,000 CFP units from reserves in 2016.

Project-funded budget 2016

47. Compared to the revised 2015 budget of 77.851 million CFP units, the 2016 project budget is forecast to be significantly lower at 58.690 million CFP units. The green book includes a three-year project income forecast in Annex 4. It also provides further information on project funding by development partner. In 2016, members contribute 12.08 million CFP units (20.6%) with development partners providing 44.225 million CFP units (75.4%) of project funding. The European Union (EU) is anticipated to be the single largest project donor with 33.82 million CFP units (36.2%), followed by Australia at 10.05 million CFP units (17.1%).
48. SPC's policy is to include in its budget only projects for which formal approval has been given at the time of budget preparation. The secretariat's forecast of project funding therefore tends to be conservative, and an increase in project income can be expected as pipeline projects progress through appraisal processes.

2017–2018 OUTYEAR BUDGET OVERVIEW

49. The 2016 green book includes two additional years, FY 2017 and FY 2018. Budget assumptions are essentially the same as for the 2016 budget, including continuation of Australia's voluntary contribution.
50. The 2017–2018 core funding budgets are projected to be 2.597 million CFP units and 3.818 million CFP units in deficit. In casting these projections, it is assumed that operating expenditure is generally at 2016 budget levels. This is, therefore, a realistic projection and does not include new initiatives or priority areas that cannot be funded with certainty. SLT will hold discussions after CRGA to further review allocations in the 2016 budget with an eye to preparing the 2017–2018 financial years and to address priority funding requests from divisions.
51. Project management fees are shown as falling significantly in both years from 2016 levels: by 1.780 million CFP units in 2017 and 3.05 million CFP units in 2018. This is a direct result of the projected decrease in income from projects that are assured. As only assured funding is included in the budget projections and prospective funding from pipeline projects (such as EDF11) is not included, an increase in management fees is anticipated. Host grants are maintained at 2016 levels in the projections.
52. In light of these projections, SPC will need to continue to control costs internally as efficiently as possible and implement cost recovery mechanisms. In the short to medium term, the secretariat will also need to significantly increase its resource mobilisation capacity. This will require an investment of time and money but is a crucial element of SPC's sustainable financing and outreach in the future.

Progress on increasing SPC's reserves

53. CRGA 40 in 2010 approved the secretariat's proposal to build the organisation's reserves to improve its capacity to deal with temporary funding shortfalls and unforeseeable funding requirements. Target levels were agreed to be achieved by financial year 2015. This decision to increase reserves to between three and five million CFP units was endorsed by the 2012 Independent External Review.
54. In light of the financial constraints for the 2015 budget, the secretariat was not able to set aside any funds towards building SPC's reserves in the 2015 budget. However, as mentioned above, in 2016 the Secretariat has budgeted for a contribution of 700,000 CFP units to the reserves.⁴
55. The secretariat's reserves as per the approved 2014 accounts are currently 6.5 million CFP units. Taking into account the 605,000 units used to balance the 2015 revised budget, as per CRGA 43's authorisation, and the secretariat's request to use 600,000 CFP units to fund priorities and initiatives under the new Strategic Plan, the level of reserves in 2016 would be 5.3 million CFP units in total. This is well above the 4.1 million unit figure presented at CRGA 44 and the 2015 CRGA target of five million CFP units. This is due both to the contribution made by the secretariat under the 2016 budget and to surplus funds in reserves identified after a thorough review. Reserves would thus have been strengthened by 1.2 million CFP units in total over the course of FY 2015 and into FY 2016.
56. This level of reserves is nevertheless significantly less than the proposal made at the 8th Conference of the Pacific Community to proactively build SPC's reserves to a level sufficient to cover 60–90 days of operation. This is equivalent to about 16 to 25 million CFP units for a 100 million CFP unit budget. The Secretariat remains committed to pursuing this objective as a matter of business continuity and risk management.

Recommendations

57. CRGA is invited to:
 - i. note the revised 2015 budget;
 - ii. approve the proposed budget for financial year 2016;
 - iii. approve the secretariat's request to use 600,000 CFP units from reserves to fund priorities and initiatives under the new Pacific Community Strategic Plan in 2016;
 - iv. recognise the serious budgetary situation for 2017 and 2018;
 - v. acknowledge the positive efforts made by the secretariat to strengthen SPC's reserves.
 - vi. approve the secretariat's plans to further develop and implement a sustainable financing strategy, including cost recovery and priority setting mechanisms, over the next three budget cycles.

⁴ This will increase to 1.3 million CFP units should CRGA not approve the use of 600,000 CFP units to create a disposable pool of funding for new initiatives under the 2016–2020 Strategic Plan.