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PROGRAMME BUDGET FOR THE BIENNIUM 1978-1979

Presentation of the United Nations budget

Advantages and disadvantages of "semi-full budgeting"

Report of the Secretary-General

1. In paragraph 1 (c) of its resolution 32/211 the General Assembly expressed the view that one of the important problems arising in connexion with the presentation of the budget is the question of the best way of dealing with inflationary trends and currency instability in a biennial programme budget. In this context, the Assembly requested a study of the advantages and disadvantages of "semi-full budgeting" and the methods used or proposed to apply this system.

The concepts of full budgeting and semi-full budgeting

2. Full budgeting means the inclusion in the budget estimates of provision for all increases or decreases in prices and salaries that can be foreseen for the budget period under consideration. The concept - in the United Nations framework - appears to have first been taken up by the Ad Hoc Committee of Experts to Examine the Finances of the United Nations and the Specialized Agencies which was established by the General Assembly by its resolution 2049 (XX) of 13 December 1965 and which had been required, inter alia, to examine the procedures for preparing and approving budgets and on the procedures for controlling their execution. In this context, the Committee had recommended, inter alia, that in the interest of keeping to a minimum the need for revised appropriations, as well as to protect working capital funds from being used for purposes other than the one for which they had essentially been intended, "the heads of organizations should calculate the budget estimates and control obligations in such a way as to ensure that appropriations are not exceeded". 1/ Taking the underlined portion of this recommendation into account, the Consultative Committee on Administrative Questions (CCAQ) subsequently recommended that full budgeting was clearly in the interests of the full implementation of programmes and that all organizations should move

1/ Official Records of the General Assembly, Twenty-third Session, Annexes, agenda item 80 (A/6343), para. 39.

towards the application of the principle as rapidly as possible. The position taken by CCAQ was subsequently endorsed by the Administrative Committee on Co-ordination (ACC), as recalled by that body as recently as in its Annual Report for 1976-1977 (E/5973), in paragraph 109 of which it expressed the view that "only if this concept is fully applied can the organizations carry out their approved programmes while avoiding or minimizing the need for supplementary estimates".

3. The concept of semi-full budgeting implies an approach whereby, in view of the uncertain nature of inflationary trends and to provide a firmer hedge against either under- or over-budgeting on that score, no attempt is made in the initial estimates to cover full potential needs resulting from inflationary cost increases. Rather, complementary action thereon is left to a later stage. As a practical example of this method, the Advisory Committee, in the introduction to its report on the proposed programme budget for the biennium 1976-1977, 2/ mentioned the budget presentation of UNESCO. UNESCO makes provision for inflation in the first year of the biennium, but not for any further inflation in the second year, and this provision is made in a global amount called an "appropriation reserve" which may be utilized only for the intended purpose and only with the prior approval of the Executive Board of UNESCO. This methodology and its practical implications are discussed in more detail in paragraphs 10 through 14 below.

#### Evaluation of the full-budgeting approach

4. When the full-budgeting method was first proposed by the Ad Hoc Committee of Experts to Examine the Finances of the United Nations and the Specialized Agencies the main objective was to keep to a minimum the need for revised appropriations. However, in a far broader perspective, attention deserves to be given to the consideration that meaningful programme budgeting requires that full cost implications be available at the time particular activities are decided upon, this being a prerequisite for ensuring from the very outset that adequate resources will be available to permit full and effective programme implementation. Having made such full provision, it follows that any additional requirements which may nevertheless arise should be met to the maximum extent possible from within the approved appropriations. In this context the Ad Hoc Committee stressed in its report that "unavoidable increases in expenditure in certain sectors should, as far as possible, be financed in the first instance by savings in other sectors". 3/ Recognizing that such a concept would be too rigid without some degree of flexibility the Committee further stated that "a special appropriation line might, where necessary, be included in the budget for these minor contingent expenses". 4/

5. It has, of course, to be borne in mind that when these recommendations were made in 1966, the impact of inflation was far less significant than in recent years and the present phenomenon of currency instability basically did not exist at all. In fact, as shown by the following statistics, requests for revised appropriations in the case of the United Nations, relatively speaking, only began to assume significant proportions as from 1973, and attributable, to an increasing extent each year, to currency instability and inflation:

2/ Official Records of the General Assembly, Thirtieth Session, Supplement No. 8 (A/10008).

3/ Official Records of the General Assembly, Twenty-third Session, Annexes, agenda item 80 (A/6343), para. 40.

4/ Ibid., para. 41.

Record of supplementary estimates submitted  
during the 10-year period 1966-1976

	Initial appropriation	Supplementary estimates	Revised appropriation
	\$	\$	\$
1966	121 567 420	(486 890)	121 080 530
1967	130 314 230	2 769 770	133 084 000
1968	140 430 950	1 356 800	141 787 750
1969	154 915 250	2 052 050	156 967 300
1970	168 420 000	536 950	168 956 950
1971	192 149 300	2 478 500	194 627 800
1972	213 124 410	(4 474 210)	208 650 200
1973	225 920 420	7 899 954	233 820 374
1974		65 560 000	
1975		<u>6 517 000</u>	
1974-1975	540 473 000	72 077 000	612 550 000
1976		38 119 100	
1977		<u>5 556 000</u>	
1976-1977	745 813 800	<u>43 675 100</u>	789 488 900

Analysis by main contributory factor of annual increases  
during the five-year period 1973-1977

	Currency	Inflation	Other	Total
	\$	\$	\$	\$
1973	10 920 500	-	(3 020 546)	7 899 954
1974	14 344 000	27 556 000 <u>a/</u>	23 660 000 <u>b/</u>	65 560 000
1975	11 078 900	1 768 400	(6 330 300)	6 517 000
1976	8 669 300	(682 000)	30 131 800 <u>c/</u>	38 119 100
1977	5 727 800	1 655 300	(1 827 100)	5 556 000

a/ Because of highly fluid economic circumstances prevailing at the time of the preparation of the initial estimates for the biennium 1974-1975, requests for additional appropriations were deferred.

b/ Includes financial implications of decisions taken by the General Assembly at its twenty-ninth session.

c/ Includes financial implications of decisions taken by the General Assembly at its thirty-first session.

Total provisions made under the regular budget for  
inflation and variations in rate of exchange in  
respect of the period 1974-1979 (estimated)

	Currency	Inflation	Total
	\$	\$	\$
1974-1975	33,500,000	55,700,000	89,200,000
1976-1977	34,200,000	83,600,000	117,800,000
1978-1979	40,700,000	96,300,000	137,000,000

6. The economic instability and rapid inflation indicated by these statistics have obviously made it more and more difficult to make realistic budgetary forecasts. The problem has been compounded by the introduction of a biennial budget period, since the projections made for the second year of the biennium are likely to be less certain than those for the first. But this aspect, in the final analysis, is not in itself an argument in favour of a semi-full budgeting approach. Uncertainty in one degree or another is inherent in any budgetary forecast and must, therefore, be accepted as an unavoidable element of the budgeting process. The necessity to base budgetary estimates on assumptions finds its corollary in the subsequent need for careful monitoring of budgetary expenditures according to actual developments.

7. The Ad Hoc Committee of Fourteen, having encouraged full budgeting in the interest of remaining within the initial appropriations, also implied that, in the event actual cost increases in the course of the financial period exceeded the levels on which the appropriations had been based, the situation should be dealt with to the maximum extent by the imposition of expenditure controls. This concept was elaborated by the Ad Hoc Committee by stating that unavoidable increases in expenditure in certain sectors should, as far as possible, be financed in the first instance by savings in other sectors. It is clear, however, that the prospects of offsetting such increases by means of either savings or contingency provisions depend decisively upon the magnitude of the budgetary impact of inflation and currency instability. This impact, as noted in paragraph 5 above, has assumed far greater proportions than anything the Ad Hoc Committee could have in mind when it wrote its report in 1966. There is a limit to the savings which can be achieved by "reassessment of priorities, redeployment of resources and, where necessary, by adjustments within the budget", without risking disruption of programme delivery. Moreover, in view of the unpredictability of a factor such as potential losses on exchange, it would be difficult if not impossible to arrive at a contingency provision which would be realistic enough and at the same time be acceptable to Member States. As true as it is that the instability of economic conditions has reached proportions which has not permitted the full achievement of the main objective of full budgeting - that is, to keep to a minimum, if not to avoid, the ultimate need for revised appropriations - this does not detract from the useful

purposes served and secured by the full-budgeting approach. As stated in paragraph 4 above, it would detract from the merits of the Organization's programme budget if no attempt were made to quantify the full potential financial impact of proposed activities prior to their approval. Indeed such a procedure, in itself, imposes a psychological constraint in the initial formulation of budgetary requirements. Thus, in order to inspire confidence in the integrity of the initial budget estimates it has become a well-observed practice to proceed, on the one hand, on the basis of the best available assumptions as to the anticipated rates of inflation while, on the other hand, keeping such rates to the most conservative levels possible. In this regard, experience has proved that it is possible to provide for the effects of inflation in this fashion with a reasonable degree of accuracy. The same cannot be said for rates of exchange as they are completely unpredictable, making it necessary, therefore, to base initial estimates on the last known rates, often requiring substantial revision in due course.

#### Evaluation of the semi-full budgeting approach

8. The argument could be made that an advantage of the semi-full budgeting approach would be a more realistic evaluation of the impact of inflation during the second year of the biennium by postponing the calculation of these requirements for a year. However, there are two principal disadvantages to such a procedure. Firstly, the submission of budget estimates in two stages would detract from the concept of a unified and complete budget submission for the whole financial period under consideration. A submission along the latter lines is the only way of providing those who have to approve the budget in the first place with the most accurate possible assessment of the total resources which would be needed for the full implementation of the various programmes once they have been decided upon. Secondly, the practical advantages of a biennial budget cycle would be dissipated to a large extent if, in order to make adequate provision for inflation, it were ever to become necessary to resubmit at the end of the first year, in every detail under all sections of the budget, such revised requirements for the second year as may prove necessary because of the initial semi-full-budgeting approach. In that context, it should be borne in mind that programme delivery and, consequently, the corresponding spending of the resources approved for the biennium do not occur in equal parts during each year of the biennium. Therefore, if a precise forecast of the inflationary impact on the second year of the biennium were required, it would be necessary to have at hand a precise breakdown of the approved resources already spent or committed in order to obtain the proper basis on which to calculate the inflationary impact for the second year. As a practical matter, however, the accounting records for the first year of the biennium would not be available at the time of the General Assembly session that year, when decisions thereon would have to be taken.

9. In addition, a procedure requiring a detailed discussion by the Fifth Committee, for the purpose of deciding on appropriations to meet the impact of inflation for the second year of the biennium, would entail reverting to the presentation of the performance report for the first year in the form which the General Assembly decided to abandon at the thirty-second session. In the light of that decision the Secretary-General intends to deal in the performance report to

be submitted to the General Assembly at its current session with only the more significant variations in initially-assumed inflation rates and rates of exchange, the main reason for requesting net additional resources at an earlier stage for the affected programmes being that serious cash shortages or over-spending of existing appropriations towards the end of the biennium might otherwise ensue. A complete calculation of the revised requirements for all programmes and all objects of expenditure and taking all contributory factors into account will therefore be postponed to the final performance report on the 1978-1979 biennium to be submitted to the General Assembly at its thirty-fourth session.

#### The UNESCO concept

10. As the only organization applying the concept of semi-full budgeting is UNESCO, an analysis of that organization's practice might serve to place the matter in a clearer perspective. In UNESCO's budget the estimated requirements at the programme level are expressed at cost rates identical to those on which the appropriations for the preceding biennium were initially based. At the section (appropriation) level, these requirements are re-costed at the rates expected to be in effect at the beginning of the new biennium, i.e., taking fully into account the cumulative impact of inflation and variations in the rates of exchange during both years of the preceding biennium. Anticipated further inflation during the new biennium is dealt with in a separate lump-sum provision entitled an "appropriation reserve" on a so-called semi-full budgeting principle as follows:

(a) Full provision for the first year of the biennium using the average rate of increase which is expected to occur during that year; and

(b) Partial provision for the second year of the biennium by carrying forward the rates expected to be in effect at the beginning of that second year, but refraining from assuming any further average rate of increase beyond that point.

11. In addition to the "appropriation reserve", which may be utilized only to cover cost increases attributable to inflation and only with the prior approval of the Executive Board of UNESCO, the approved budget contains a separate contingency provision to cover possible additional requirements as a result of variations in the rate of exchange.

12. If one compares the aforementioned approach with that followed by the United Nations, it may be said that the United Nations budget costing technique is based on the formula: average costs prevailing during second year of preceding biennium + average anticipated increase during first year of new biennium + average further cost increase during second year of the new biennium, whereas UNESCO's approach amounts to the following: cost levels expected to be reached by the first day of the new biennium + anticipated cost increase during first year + cost levels reached by end of first year projected to the end of second year. The fact that in the case of each year of its biennium UNESCO builds on a higher base than the United Nations not only ensures a significant reserve capacity to meet

rising costs during the biennium as a whole, but diminishes the actual impact of omitting provision for further inflation during the second year. Thus of the total percentage increase of 22.8 per cent in the level of the budget proposed for UNESCO for the biennium 1979-1980, the Director-General has attributed 16.9 per cent to inflation. Moreover, it has been indicated by the UNESCO secretariat that full provision for such further inflation would have necessitated the addition of \$5 million or less than 2 per cent to its proposed budget of \$275.5 million for the biennium 1979-1980.

13. Another special feature of UNESCO's methodology, as already noted in paragraph 10 above, is that the provision made for further inflation beyond the cost levels expected to be in effect at the beginning of the biennium is appropriated in a global amount in a separate part of the budget resolution. This "appropriation reserve" can be drawn upon only with the prior approval of UNESCO's Executive Board and only for the purpose of covering increases in prices and staff remuneration. It has been ascertained that UNESCO normally issues allotments at the beginning of each year of the biennium based on approved expenditure plans but excluding any part of the appropriation reserve. Submissions regarding the use of that reserve are made to the Board twice a year, at its spring and autumn sessions, respectively. These submissions take the form of a report on cost increases which have actually occurred and a request for authority to transfer the additional resources from the reserve to the various other parts of the budget in the required amounts. This frequency has sufficed up to now since UNESCO has been able to finance particular cost increases on a temporary basis by advances from funds earmarked for the rest of the biennium for other purposes within the same appropriation line. It would appear, therefore, that consideration of these matters by the Board is a fairly routine procedure based on the acceptance by the Board of accomplished facts.

14. As to the constitutional implications of the policy of semi-full budgeting as practised by UNESCO, there is no evidence that the General Conference intended to impose upon the Director-General an absolute obligation to absorb the potential short-fall in the resources at his disposal. Given the modest extent of the under-budgeting involved, the experience has been that, by and large, actual expenditures under each appropriation line have coincided with the original appropriation line plus transfers from the reserve. During the last three biennia supplementary estimates were requested to meet deficits due primarily to losses on exchange. It is also significant to note in this regard, that the Executive Board, which normally meets twice a year, is empowered to authorize additional expenditures up to 7.5 per cent of the appropriations approved by the General Conference.

#### Conclusions

15. Whether the United Nations would derive any benefit from adopting any or all of the procedures followed by UNESCO depends on the objectives to be pursued by such a course of action. The Advisory Committee on Administrative and Budgetary Questions in raising the matter appears to have had in mind the question of how under-budgeting or over-budgeting might more effectively be avoided. This is

borne out by the comment made by the Chairman of the Advisory Committee on the same subject in his statement to the Fifth Committee on the proposed programme budget for 1978-1979 as follows:

"... the experience of rapid inflation leads one to conclude that in projecting future budgetary requirements for these factors either too much or too little can be projected". 5/

In a related observation, the Advisory Committee implied that expenditures due to inflation might be kept under closer control if, as in the case of UNESCO, the provisions for this purpose were to be segregated in a separate part of the budget from which it could be distributed to other parts only with the consent of a governing organ. The UNESCO experience is not very indicative on this point, largely because, as described in paragraph 12 above, the particular methods followed by that organization in calculating the effects of inflation, even on a less than complete basis, in fact fall only a little short of stating the full potential needs for covering the impact of inflation. Even though in the case of the United Nations this discrepancy would be more significant, it is submitted that experience has shown that, on the whole, it has been possible to provide for the effects of inflation, if not those of variations in the rates of exchange, with a fair degree of accuracy. While in many cases events have proved that the initial assumptions made in this regard were too conservative, there have been compensatory factors which have significantly reduced the need for additional appropriations for this particular purpose. On the whole, comparing the complexity of a semi-full budgeting approach with what would be actually gained therefrom, it appears that, in the context of an integrated programme and budget system, a full-budgeting approach offers significant advantages.

16. The next question would be whether expenditures due to inflation would be kept under closer control if they were provided for under a separate section of the budget and could not be effected without the prior approval of a governing body, which, in the case of the United Nations, would probably be the Advisory Committee acting on behalf of the General Assembly. UNESCO's practice in this regard is described in paragraph 10 above. In that organization's case, the special functions entrusted to its Executive Board, meeting twice a year, are explained, to some extent, by the fact that its General Conference meets only every second year. It is for this reason, for instance, that the Board has the authority to authorize additional expenditures up to 7.5 per cent more than those envisaged in the appropriations. In the case of the United Nations, the Advisory Committee also has extensive authority, in accordance with the provisions of the customary resolution on unforeseen and extraordinary expenses, to act on the General Assembly's behalf. However, the Assembly meets annually and receives annual budget performance reports on the basis of which it can monitor expenditures attributable to inflation and itself make the necessary adjustments by revising the existing appropriations. Moreover, it appears, as noted in paragraph 13 above, that the controls exercised by the Board are more apparent than real. Whatever advantage one might expect from adopting similar procedures for the United Nations, it would be very much outweighed by the drawbacks of splitting the provisions for individual programmes between one section containing the programme requirements as such, and another section reserved for the appropriations for inflation. Not only would there be a risk of understating the cost of the various programmes, but complications would result in respect of the allotment and accounting processes.



17. The further question remains, raised by a number of representatives in the Fifth Committee in the course of the general debate on the 1976-1977 budget, whether the introduction of semi-full budgeting might not be an effective means of encouraging restraint and more austere management of scarce resources on the part of the Secretariat. In the first instance, if one wishes to refer in this respect to the practice of UNESCO, it should be noted, as indicated in paragraph 14 above, that its Director-General has not been placed under any absolute obligation to absorb any potential short-fall in the resources at his disposal as a result of the semi-full budgeting approach followed in determining the level of appropriations, although it may certainly be expected that he should make the attempt. The second consideration, as already referred to in paragraph 7 above, is that the prospect of absorbing the effects of inflation within existing resources without detriment to programme delivery depends inevitably on the amount involved. If the United Nations had followed UNESCO's example and made no provision for further inflation during the second year of the current biennium, it is estimated that the initial appropriation of \$985.9 million for the biennium 1978-1979 could have been reduced by some \$20 million or a little more than 2 per cent. <sup>6/</sup> This happens to be more than the total adjusted real growth of \$17.2 million for which provision was made in those appropriations and could obviously not have been omitted without serious impediment to the effective implementation of programmes.

18. There can be no question as to the desirability of the greatest possible accuracy in the estimation of the effects of inflation and of restraint in the implementation of the budget, including maximum absorption of cost increases by such economies as do not impair the integrity of work programmes. However, from the foregoing analysis of the advantages or disadvantages of semi-full budgeting, it would appear that these objectives could be met to greater effect by further improvement of estimating techniques, by careful monitoring of actual experience during the biennium and by adjustment in the annual performance reports, all within the present system of full budgeting as endorsed by the Administrative Committee on Co-ordination and under regular interagency review.

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<sup>6/</sup> This estimate relates to the effects of inflation alone. Losses on exchange for which, unlike UNESCO, the United Nations makes no contingency provision, will require substantial additional appropriations this biennium.