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FINANCE COMMITTEE

Hundred and Forty-third Session
Rome, 7 - 11 May 2012
2011 Actuarial Valuation of Staff-Related Liabilities

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EXECUTIVE SUMMARY

- This document is presented in two parts: Part A and Part B.
- Part A 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 2011.
- 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*** summarizes the total liability of the Plans as at 31 December 2011, 2010 and 2009 and provides the key assumptions used in those valuations. During 2011 the total liabilities of the Plans increased by a nominal amount of USD 2.2 million from USD 1,149.8 million at 31 December 2010 to USD 1,152.0 million at 31 December 2011. This increase was limited and the various reasons for the change are understood and in line with expectations.
- 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 2011, 2010 and 2009, respectively. The total unfunded liability of the Plans as at 31 December 2011 was USD 817.7 million compared to USD 824.9 million at 31 December 2010.
- Section IV. ***Accounting and Funding*** provides comparison of the annual Current Service Costs for the Plans for the three years ending 31 December 2012. The Current Service Cost for 2012 is USD 38.8 million (2011 – USD 35.0 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 24.6 million, while the funding approved by Conference for 2012 and 2013 amounted to USD 7.05 million per year leaving a shortfall of USD 17.55 million per year. The annual past-service TPF funding amortization to fully fund the liability by 2025 amounts to USD 5.9 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.
- Part B of this document responds to the request of the Committee at its 143rd Session to study *Alternative Long Term Strategies and Options for Funding Staff Related Liabilities*. The focus of this study is exclusively on After Service Medical Coverage (ASMC) as it accounts for almost 85% of all Staff Related Liabilities.

GUIDANCE SOUGHT FROM THE FINANCE COMMITTEE

- The Committee is invited to note the results of the 2011 actuarial valuation and the current financial situation, accounting and funding of the Organization's liability for staff-related plans at 31 December 2011. The Committee is invited to report to Council the biennial funding amounts necessary to fully fund the liabilities by 2040 (ASMC) and 2025 (TPF).
- The Committee is invited to review the results of the study of Alternative strategies and options for funding staff related liabilities and report to Council on the conclusions of its review.

Draft Advice

- **The Finance Committee reviewed the results of the 2011 actuarial valuation and noted the amounts necessary to fully fund the ASMC and TPF past service liabilities by the target years of 2040 and 2025, respectively. The Finance Committee also reviewed the**

results of a study of Alternative strategies and options for funding staff related liabilities. 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 underfunded. 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.**
3. **The reductions in the liability identified with the performance of the Medical Insurance Plans reflect a clear strategy aimed at cost containment and urged the Secretariat to continue with these efforts.**
4. **FAO's Medical Insurance Plans are generally in line with those of other UN Organizations in terms of eligibility, coverage and cost-sharing.**

PART A

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.

3. The actuarial valuations for 2011, 2010 and 2009 were all performed by Aon Hewitt (www.aon.com).

4. The results of 2010 actuarial valuation of the Plans were reported to the Finance Committee in March 2011[1] (2010 Actuarial Valuation of Staff-Related Liabilities - doc. FC138/4). This document refers to the results of the actuarial valuation as at 31 December 2011 and the current financial situation, and accounting and funding of the Organization's liability with comparative information as at 31 December 2011, 2010 and 2009.

Results of Actuarial Valuations

5. A comparison of the total actuarial liability by plan as at 31 December 2011, 2010 and 2009 is detailed in Table 1.

[1] 138th Session of the Finance Committee.

Table 1

(in USD Millions)

Plan	2011	Increase/ (Decrease) USD m	%	2010	Increase/ (Decrease) USD m	%	2009
CPRF	19.0	*1.4*	*8.0%*	17.6	*(0.4)*	*-2.2%*	18.0
TPF	67.3	*6.5*	*10.7%*	60.8	*2.6*	*4.5%*	58.2
SPS	86.7	*(2.1)*	*-2.4%*	88.8	*(11.3)*	*-11.3%*	100.1
ASMC	979.0	*(3.6)*	*-0.4%*	982.6	*48.1*	*5.1%*	934.5
Total actuarial liability	**1,152.0**	***2.2***	***0.2%***	**1,149.8**	***39.0***	***3.5%***	**1,110.8**

6. As detailed in Table 1 above, the net increase of USD 2.2 million in the actuarial liability between 2011 and 2010 was limited and the various reasons for the change are understood and in line with expectations. Whilst the total net increase was minimal, there were significant variations relating to the assumptions and methods as follows:

Sources of Changes	**Variation USD m**
Expected change related to accrual of current service and interest cost	42.6
Change in discount rates	122.7
Movement in Euro-USD exchange rate	(13.1)
Claims and administrative expenses experience	(50.0)
Change in age grading assumption	(28.2)
Increase in assumed post-retirement lapse rates	(22.7)
Decrease in assumed medical trend rates	(24.2)
Decrease in assumed organization share of cost	(30.6)
Others	5.7
Total net increase	2.2

7. 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 2011 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 2011, 2010 and 2009 are presented below in Table 2.

Table 2

	Key Assumptions	2011	2010	2009
	Economic			
1	Discount rate			
	ASMC	4.3%	5.0%	5.4%
	SPS	4.3%	4.7%	5.1%
	TPF	4.4%	5.3%	5.8%
	CPRF	4.4%	5.5%	5.9%
2	Medical cost inflation rate	4% for 2012 to 2014, and 5% thereafter	5% starting from 2011	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	1.29	1.31	1.44

Current Financial Situation

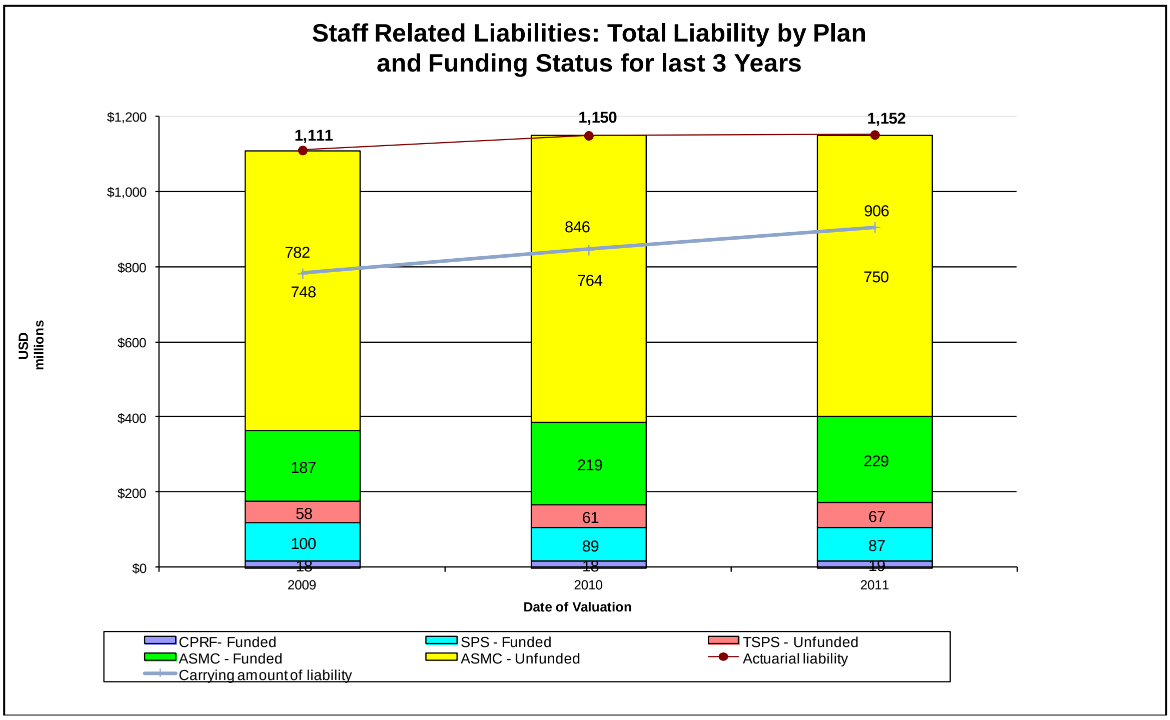
8. Table 3 and Graph 1 below show the total recorded and unrecorded liabilities[2] for the Plans based on the actuarial valuations, as well as the total funded and unfunded liabilities[3] for all Plans as compared to the fair market value of earmarked long-term assets[4] at 31 December 2011, 2010 and 2009, respectively.

Table 3

(in USD Millions) Plan	2011	*% of total liability*	2010	*% of total liability*	2009	*% of total liability*
CPRF	19.0	*1.6%*	17.6	*1.5%*	18.0	*1.6%*
TPF	25.9	*2.2%*	22.9	*2.0%*	21.1	*1.9%*
SPS	85.2	*7.4%*	88.5	*7.7%*	89.6	*8.1%*
ASMC	775.9	*67.4%*	714.6	*62.1%*	653.7	*58.8%*
Total accrued liabilities	**906.0**	*78.6%*	**843.6**	*73.4%*	**782.4**	*70.4%*
Add: Unrecorded liabilities	246.0	*21.4%*	306.3	*26.6%*	328.4	*29.6%*
Total actuarially determined liabilities	**1,152.0**	*100.0%*	**1,149.9**	*100.0%*	**1,110.8**	*100.0%*
Less: Earmarked long-term investments (at Fair Market Value)	(326.8)	*28.4%*	(316.3)	*27.5%*	(294.8)	*26.5%*
Less: Advances to staff on SPS	(7.5)	*0.7%*	(8.7)	*0.8%*	(10.1)	*0.9%*
Total unfunded liabilities *	**817.7**	*71.0%*	**824.9**	*71.7%*	**805.9**	*72.6%*
* Of which:						
TPF	67.3		60.8		58.2	
ASMC	750.4		764.1		747.7	
Total unfunded liabilities	**817.7**		**824.9**		**805.9**	

[2] Recorded liabilities totaled USD 906.0 million at 31 December 2011. Unrecorded liabilities of USD 246.0 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 817.7 million at 31 December 2011.
[4] Earmarked long-term assets include outstanding advances to staff members on final Terminal Emoluments.

Graph 1



9. As shown in Table 3, the Organization has deferred recognition of USD 246.0 million of the actuarially determined liability as at 31 December 2011. 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 of USD 246.0 million deferred, USD 203.1 million (2010 – USD 268.1 million) relates to ASMC; USD 41.4 million (2010 – USD 37.9 million) relates to TPF; and USD 1.5 million (2010 – USD 0.3 million) relates to SPS.

10. 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.

11. During 2011, the carrying value of long-term investments earmarked by the Organization for the Plans increased by USD 3.1 million from USD 316.3 million at 31 December 2010 to USD 326.8 million at 31 December 2011. For comments on investments, reference should be made to the separate paper FC 143/5.

Accounting and Funding

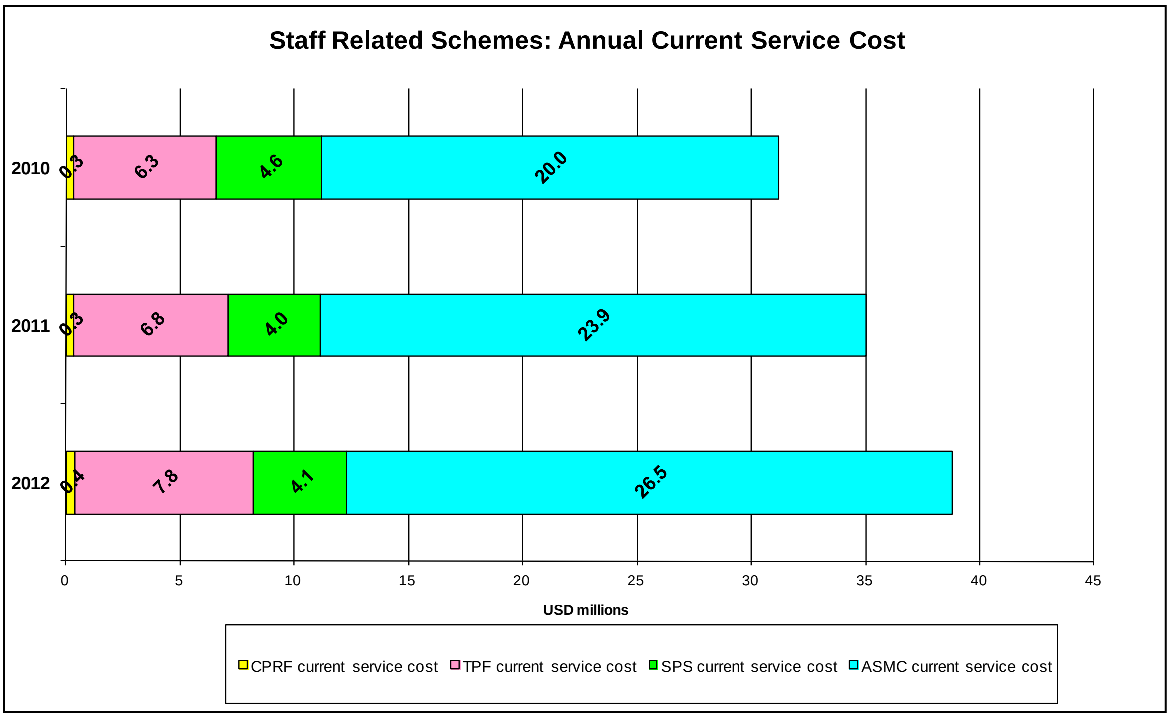
12. Table 4 and Graph 2 below show the annual Current Service Costs[5] for the three years ending 31 December 2012, which are based on the actuarial valuations for the preceding years at 31 December 2011, 2010 and 2009, respectively.

[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

Table 4

(in USD Millions)						
Plan	**2012**	***% total expense***	**2011**	***% total expense***	**2010**	***% total expense***
CPRF	0.4	*1.0%*	0.3	*0.9%*	0.3	*1.0%*
TPF	7.8	*20.1%*	6.8	*19.4%*	6.3	*20.2%*
SPS	4.1	*10.6%*	4.0	*11.4%*	4.6	*14.7%*
ASMC	26.5	*68.3%*	23.9	*68.3%*	20.0	*64.1%*
Total	**38.8**	***100.0%***	**35.0**	***100.0%***	**31.2**	***100.0%***

Graph 2



13. The increase in the total current service cost is mainly due to ASMC. The reasons for this are:

- increase of USD 4.9 million due to the change in the discount rate from 5.0% to 4.3%;
- increase of USD 2.3 million due to new entrants to the Plan in 2011; and
- offset by various decreases of USD 4.6 million including claims and administrative expense experience and change in age grading assumption.

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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.

14. 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 2011, 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	19.0	17.6	18.0
SPS	86.7	88.8	100.1
Partially funded			
ASMC	228.6	218.6	186.8
Unfunded			
TPF	0.0	0.0	0.0
Total funded liabilities	**334.3**	**325.0**	**304.9**
Funded by:			
Earmarked long-term investment	326.8	316.3	294.8
Advances to staff on SPS	7.5	8.7	10.1
	334.3	**325.0**	**304.9**

15. 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.

16. Based on the most recent actuarial valuation as of 31 December 2011, in order to fully fund the TPF past service liability of USD 67.3 million (using a 15-year amortization period starting in 2010), the Organization would need to contribute an additional USD 5.9 million per year (USD 11.8 million per biennium).

17. Based on the most recent actuarial valuation as of 31 December 2011, in order to fully fund the US Dollar value of the unfunded ASMC past service liability of USD 750.4 million (using a 30-year amortization period beginning in 2010), USD 24.6 million per year (USD 49.2 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 2012-13 currently amount to USD 7.05 million per year (USD 14.1 million per biennium) as approved by Conference in June 2011. 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

18. 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 later in 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*".

19. For information purposes, Table 6 below shows a comparison of the ASMC liability of UN system organizations at 31 December 2010, 2009 and 2008.

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-08	31-Dec-09	31-Dec-10	31-Dec-08	31-Dec-09	31-Dec-10	31-Dec-08	31-Dec-09	31-Dec-10	31-Dec-08	31-Dec-09	31-Dec-10
FAO	878.0	934.5	982.6	141.0	186.7	218.6	596.0	653.6	714.5	282.0 (a)	280.9 (a)	268.1 (a)
IAEA	225.0	244.0	244.0	-	-	1.0	-	-	145.0	225.0	244.0	99.0
ICAO	46.8	54.2	65.8	-	-	1.4	-	-	65.8	46.8	54.2	-
IFAD	50.0	61.3	56.2	57.0	60.0	66.8	50.0	61.3	56.2	-	-	-
ILO	499.4	509.5	564.0	27.9	36.2	40.0	-	509.5	564.0	499.4	-	-
IMO	22.7	26.7	27.2	-	3.3	-	-	-	27.2	22.7	26.7	-
ITC	53.8	37.1	-	-	-	-	53.8	37.1	-	-	-	-
ITU	-	188.0	-	-	-	-	-	-	-	-	188.0	-
PAHO	167.0	202.6	257.7	18.3	22.3	24.6	-	-	186.5	148.8	180.3	71.2
UN	2,596.0	2,302.5	-	-	-	-	2,596.0	2,302.5	-	-	-	-
UNDP	502.9	430.3	-	320.2	373.3	-	302.2	373.3	-	182.7	57.0	-
UNCDF	-	10.6	-	-	-	-	-	-	-	-	10.6	-
UN WOMEN	-	20.2	-	-	-	-	-	-	-	-	20.2	-
UNESCO	-	649.0	735.6	-	27.2	-	-	-	735.6	-	649.0	-
UNFPA	72.8	87.5	87.5	70.0	79.0	84.5	72.8	87.5	87.5	-	-	-
UNHCR	307.8	347.4	-	-	-	-	307.8	347.4	-	-	-	-
UNICEF	483.0	464.0	507.0	180.0	210.0	240.0	-	-	-	483.0	464.0	507.0
UNIDO	104.9	100.5	124.0	-	-	-	-	-	124.0	104.9	100.5	-
UNRWA	-	-	-	-	-	-	-	-	-	-	-	-
UNWTO	3.4	3.8	3.8	-	-	1.1	-	-	1.1	3.4	3.8	2.7
UPU	5.6	5.6	-	-	-	-	-	-	-	5.6	5.6	-
WFP	165.2	181.8	203.7	93.5	107.4	112.8	165.2	181.8	203.7	-	-	-
WHO	-	1,000.0	1,365.0	-	450.0	478.0	-	450.0	478.0	-	550.0	887.0
WIPO	73.9	98.9	112.0	-	-	-	36.8	45.5	101.0	37.1	53.4	11.0
WMO	75.0	59.5	65.2	1.3	1.7	-	-	-	65.2	75.0	59.5	-

(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 liabilitie

PART B

20. PART B of this document responds to the request of the Committee at its 143rd Session to study *Alternative Long Term Strategies and Options for Funding Staff Related Liabilities*. The focus of this study is exclusively on After Service Medical Coverage (ASMC) as it accounts for almost 85% of all Staff Related Liabilities. The document is presented under the following Sections.

21. Section ***I. Introduction*** describes the BMIP/MMBP plans, providing a further breakdown of the components of ASMC Liability and how these have evolved in recent years and the various cost containment initiatives that have lowered the claims cost and thus the Actuarial projections of ASMC liability.

22. Section ***II. FAO Medical Insurance Plans (BMIP/MMBP) vis a vis other UN Organizations*** compares key indicators of FAO's Medical Plans with that of other UN agencies and breaks down the ASMC liability on a per capita basis. FAO's Medical Insurance Plan, in terms of coverage and eligibility, is in line with that of other UN agencies and the unfunded liability on a per capita basis is often below the average of that of 7 other UN agencies.

23. Section ***III. Potential Long Term Strategies*** highlights the strategies being considered by various UN agencies. These involve the use of national insurance programs, increased payroll deductions, increased budget allocations and cash injections. All strategies have potential drawbacks, mainly increased costs for the Organization or for staff members, which need to be carefully evaluated.

24. Section ***IV. Alternative Potential Long Term Strategies*** analyzes the impacts on the ASMC liability if:

- The current 10 year vesting period were increased to 12 years
- The current retirement age were increased from 62 to 65, and
- The provisions for retirees to enrol dependent parents are removed.

It should be noted that the actuarial valuation of the ASMC liability is a quantification of the present value cost of the after-service medical coverage already earned by all participants, both active and retired, and thus any changes in the plan would only have an effect in the future.

25. Section ***V. Going Forward*** briefly identifies some of the drawbacks of the options discussed and reaffirms that a supplementary assessment to fund the shortfall of the ASMC liability is still the most feasible option. Particular attention is drawn to specific recommendations in Joint Inspection Unit Report JIU/REP/2007/2, and how changes to the current plan coverage and plan structure would be contrary to the harmonization of medical insurance plans within the UN system. The concluding remark highlights the success of past and ongoing cost containment efforts to and the Organization's commitment to continue finding alternative and new cost containment measures

I. Introduction

26. The Medical Insurance Coverage for FAO/WFP staff and retirees is extended through two plans, a mandatory Basic Medical Insurance Plan (BMIP) and a complementary (optional) Major Medical Plan (MMBP). The Medical Insurance Plans (BMIP/MMBP) are split into two schemes based on the currency of the premiums; a US Dollar scheme and a Euro scheme. The valuation of the After Service medical Coverage (ASMC) liabilities does not take into account the MMBP as it is an optional plan available to staff members and retirees to which the Organization does not contribute.

27. The ASMC liability represents the present value of estimated future cash payments that the Organization will be required to make in respect of after service health insurance coverage that the employees have earned up to the date at which the liability was calculated. The liability increases as active employees annually earn more after-service coverage. The liability decreases as premiums are paid out to insurance providers for separated and retired employees.

28. The ASMC liability varies year on year and is subject to varying macroeconomic factors. Some of these factors are beyond the control of the Organization.

29. Changes to Plan Structure and Coverage of the BMIP, if applied to new Staff Members, could contain the increasing trend of the liability, but the overall ASMC liability figure would likely not decrease significantly in the short to medium term.

30. As detailed in Table 8 below, the factors that affected the increase of ASMC liabilities over the past years can be broadly classified as:

- changes in Actuarial/Accounting Assumptions beyond FAO's control
- demographics (new hires, early retirement and general age composition);
- macro-economic factors (such as discount rates and exchange rate);
- performance of the Medical Plan

31. Between 2006 and 2011 the ASMC liabilities have increased from USD 526,324,230 to USD 979,005,847, an increase of about USD 453 million, broken down as follows:

- increase of USD 216 million due to change in Actuarial/Accounting Assumptions beyond FAO's control
- increase of USD 255 million due to demographics;
- increase of USD 116 million due to macro-economic factors;
- decrease of USD 134 million due to performance of the Medical Insurance Plan

32. **The reduction in the ASMC liability attributable to the performance of the medical insurance plans is the result of a clear strategy aimed at cost containment.** If the average claims cost is lowered, this in turn has a positive effect on the actuarial projections of the ASMC liability**.** The strategy is best summarized as a three pronged approach:

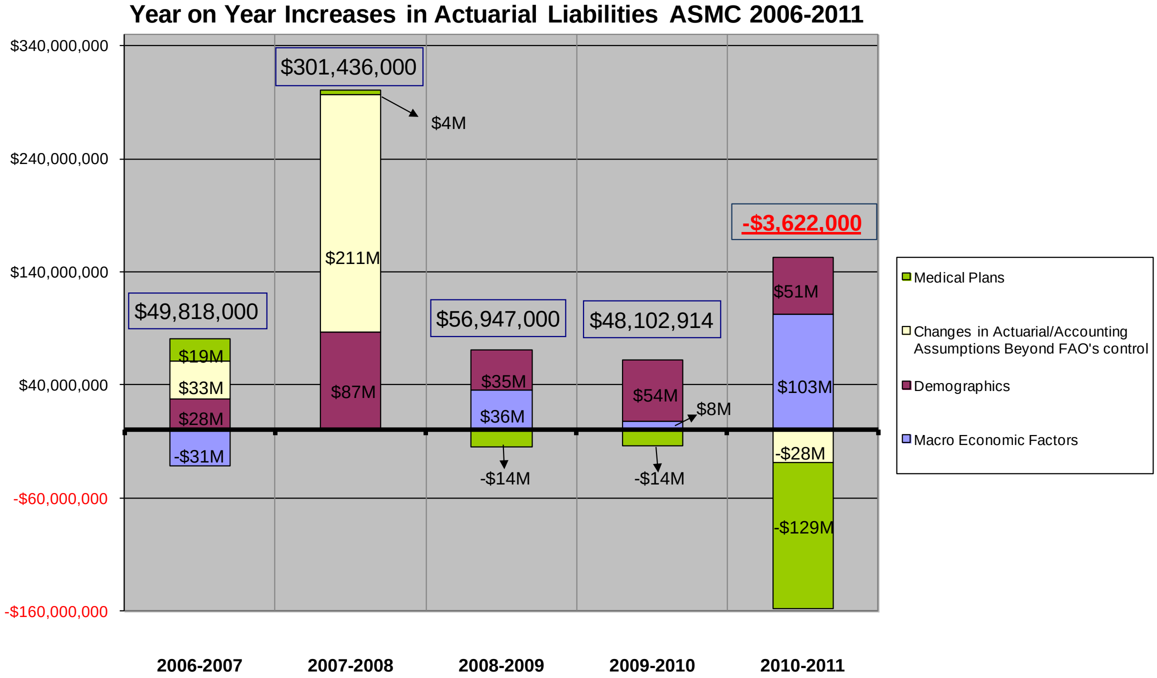
- Competitive Insurance Contract Terms
  - Insurance fees reduced in 2007 by 29% (from 4.2% to 3% of insurance premiums paid the insurers); 2010 by 18% (from 3% to 2.45%) and by a further 6% to 2.3% following the reductions negotiated for the 2012-2014 contract extension
  - Annual Claims Handling Fees reduced from approximately USD 513 per capita in 2008 to a projected USD 398 per capita in 2014, a reduction of 22.4%, following the reductions negotiated for the 2012-2014 contract extension
  - Latest negotiations generated estimated savings to the Organization’s share of premium of approximately USD 100,000 per annum.
- Continuous Review of the Plan Design and Structure
  - Increased threshold for voluntary complimentary plan in 2009, reducing Organization’s share of premiums by approximately USD 100,000 per annum.
  - Adjusting caps on Retirees’ contributions in 2009 reducing Organization’s share of premiums by approximately USD 250,000 per annum.

- Mitigation of increase in Treatments (Claims) Costs
    - The mitigation of claims containment is an integral part of the contract and there are inflation specific SLA targets placed on the claims administrator. This has resulted in the implementation of initiatives which have drastically contained costs.
    - Below is a Table 7, extracted from the 2010 Cost Containment Report which highlights the various initiatives and the overall savings obtained for that year and compares the total with the previous year. The 2011 Cost Containment Report is yet to be released but we expect strong savings in light of the switch from UHC to CIGNA as the Third Party Administrator in the USA as well as two new discount agreements with pharmacies in Rome.

Table 7

Item	**Savings (USD[**])**
Hospital network Italy	827,209
Out-Patient Doctor Network Italy (direct payment only)	191,427
Hospital Network other countries (as mentioned on invoices)	405,044
Case management (cases closed 2010)	382,792
Travel provision	76,685
Reasonable and customary out-patient	173,333
Reasonable and customary in-patient	567,099
Third Party Administrator USA	3,149,680
Pharmacy Network USA	507,054
Preventive program: colonoscopy	29,957
Preventive program: mammography	46,061
Walk-in clinics	104,127
Pharmacies Rome	128,115
Out-patient centers Rome	378,359
Fraud detection	12,851
Grand Total	**6,979,784**
2009	6,373,080

Table 8



II. FAO Medical Insurance Plans (BMIP/MMBP) vis a vis other UN Organizations

33. FAO's Medical Insurance Plans are generally in line with those of other UN Organizations in terms of eligibility, coverage and cost-sharing. Table 9 provides a brief comparison of medical insurance plans offered by some UN agencies. The continuation of health insurance coverage under the BMIP/MMBP plans schemes as provided by the after-service health insurance programme is a vital element of social security for retiring staff members, most of whom are not covered by national plans, offered by all UN agencies listed in Table 9.

34. The ASMC liability of FAO is, in absolute terms, the third largest reported amongst UN Organizations as shown in Table 6. The total ASMC liability is in part a function of the number of active staff, who accrue liability on a yearly basis as they work towards the vesting period for ASMC eligibility, and retirees who opted for ASMC coverage for life.

35. Table 6 shows that in 2010, funding of ASMC liabilities ranged from 0% to 119% with an average of 23%. In comparison, FAO's available funding as per 2010 Actuarial Valuation stood at 22.25%. FAO's liability recorded on the balance sheet stood at around 73% of its total ASMC liability, against an average (of the Organizations listed in Table 6) of 66%[6].

36. Table 10 shows data collected and presented at the 2010 Insurance Officers' Forum Benchmarking exercise. The population figures refer to the 2008 and 2009 years of account with the assumption that there have not been large changes in population figures. Keeping these figures unaltered and using the 2010 ASMC liability figures, it is evident that out of the eight UN agencies for which data is available, FAO has the 3rd lowest per capita unfunded liability, despite having the 3rd largest ASMC liability (counting staff and retirees including dependents). The result can be interpreted as FAO's funding and cost efficient Medical Insurance Plans, result in a lower per capita ASMC unfunded liability, than some of the other UN agencies observed.

[6] Data from *Survey on After Service Health Insurance (ASHI)* CEB/2011/HLCM/FB/19

III. Potential Long Term Strategies

37. Most discussions on unfunded ASMC liabilities amongst the UN Organizations have focused predominantly on (1) shifting liabilities (and service costs) onto national insurance programs (2) raising capital through additional payroll charges (3) increasing budgetary allocations or (4) providing immediate cash injections. The first option is aimed at reducing the ASMC liability whilst the other options focus on funding the liability so as to decrease the unfunded portion.

38. By analyzing the per capita costs of providing national health care amongst various countries, it emerges that in most countries where UN organizations have their HQ's the per capita health financing costs, in USD adjusted of purchasing power parity (PPP), are higher than the per capita cost of FAO's BMIP/MMBP plan. Consequently, trying to find solutions which rely on National Health Schemes would simply shift the costs from the Organization to the Member States. Since the expenditure costs are greater it is safe to assume that the long term liabilities would also be greater.

39. Table 11 presents the 2009 per capita annual costs of Government Health Care expenditure, in USD PPP, of selected countries. The data, extrapolated from the OECD website, shows an average per capita cost of USD 2,412 (PPP). By contrast, using data for the same year, the per capita cost of the BMIP/MMBP plan for FAO compares favorably with USD 1,835. This is obtained as follows:

- USD 31,493,628 – FAO's share of BMIP for Staff, Retirees and Dependents in 2009 on an annual pay as you go basis.
- FAO Population in 2009: 17,165 (Staff, Retirees and Dependents)
- USD 1,835 per capita annual cost.

Moreover, different countries have different national insurance schemes, if at all. Relying on these to mitigate ASMC liabilities would create strong disparities in the level of care afforded depending where staff members work or retirees reside.

40. Raising capital through increased payroll deductions is a solution that has also been studied by some UN Agencies. This approach is geared at reducing the amount of unfunded liabilities, rather than the overall liability itself. The increased payroll charge can be funded in one of two ways:

1) It is added to staff costs. The advantage is an equitable and easy collection of funds. The disadvantage is an increase in staff costs, something most member countries and the Organization would rather avoid in current times.
2) It is implemented as an additional deduction from the remuneration of staff. Again the advantage is an easy and constant collection of money. The disadvantages are that it would reduce staff net take home pay and creates an imbalance in the 50% share of BMIP premium paid by staff.

41. An added problem, common to any form of additional payroll charge, is that only Staff Members would be affected and not retirees, as their pensions are paid by the UNJSPF, hence unaffected.

42. Increasing budget allocations would encounter the same difficulties as an additional payroll tax funded by the Organization. Although staff costs would not increase, an increase in budget allocations would reduce the available budget for other program expenses, unless the increased allocations were in the form of additional funds.

43. A one off cash injection by Member Countries is a further option that has been explored. This solution seems highly unlikely in the current economic climate given the value of funds that would be required.

IV. Alternative Potential Long Term Strategies

44. The Organization requested the actuaries for the annual actuarial valuation, to look at three potential strategies to reduce the Organization's ASMC liability:

1) increasing the Normal Retirement Age (NRA) from 62 to 65;
2) increasing the vesting period from 10 years to 12 years. This translates into staff having to participate for a minimum of 12 years in the medical plan in order to be eligible for ASMC;
3) removing the possibility of covering dependent parents of retirees.

45. With a Defined Benefit Obligation (DBO) of USD 982,628,024[7] as the baseline (value of the 2010 Actuarial Valuation) an increase in NRA from 62 to 65 would produce savings ranging from USD 2 million (about 0.2%) to USD 50 million (about 5%). Table 12 presents the four scenarios studied, providing for each scenario, details of the methodology and assumptions made. The largest potential reduction in ASMC liability is derived from Scenario 2 which assumes NRA and early retirement age would be increased for all, newcomers and existing staff members. Since it is unlikely that existing staff members will be affected, hence the potential reduction of ASMC liabilities would be significantly lower.

46. Increasing the vesting period from 10 years to 12 years, and from 20 to 22 years in the case of staff members retiring before the age of 55, would reduce the defined benefit obligation by around USD 9 million or 0.9%. The 2-year increase in the eligibility for ASMC would therefore have little impact because most staff have 12 years of service by age 55. However a larger increase in the vesting period, say 5 years, would likely produce greater savings. It should be noted, however, that all UN Agencies appear to have a 10 year vesting period, and changing this could put FAO at a competitive disadvantage particularly when looking at recruitment or transfers of professionals from another UN agency to FAO.

47. The third study looked at the potential reduction in the ASMC liability if the provision allowing for dependent parents of retirees to be covered (only under certain conditions) were removed from the plan design. On the Defined Benefit Obligation pertaining to retirees amounting to USD 620 million, the coverage extended to eligible parents represents only USD 3.2 million. This equates to an approximate 0.3% reduction in the overall ASMC liability figure if this option were pursued.

V. Going Forward

48. Reducing the coverage of the medical insurance plan would likely encounter resistance from staff members and be detrimental to FAO's ability to recruit and retain high calibre personnel compared to other UN agencies. The importance of the medical insurance plans in the overall employment package cannot be underestimated. Furthermore, any potential changes to coverage and the structure of the medical insurance plan would likely affect only new entrants to the plan, having a minimal impact on the ASMC liability.

49. A supplemental assessment to fund the remaining part of the ASMC liability over an acceptable period of time in accordance with accounting regulations and standards and as identified in the 2011 Actuarial Valuation of Staff Related Liabilities appears to be the most feasible option. Alternatively, hybrid options whereby the Organization, Member States and participants (staff members and retirees) all contribute to funding the ASMC liability shortfall could be further investigated.

50. In studying potential strategies in the near future, two key recommendations from the 2007 Joint Inspection Unit report, United Nations System Staff Medical Coverage (JIU/REP/2007/2), must be considered:

[7] This DBO is split as USD 619,614,621 pertaining to retirees and USD 363,013,403 pertaining to active staff members who have accrued the right to ASMC.

Recommendation 1
The legislative bodies of the United Nations system organizations should formally recognize staff health insurance as an important integral part of the common system. They should request the International Civil Service Commission (ICSC) to undertake periodic reviews with a view to making recommendations to the General Assembly.

Recommendation 3

The legislative bodies of each United Nations system organization should request their respective executive heads to harmonize the existing health insurance schemes, initially at the level of the duty station, and in the longer term across the common system, relating to scope of coverage, contributions and benefits and to establish periodic reporting on health insurance related information to the legislative bodies.

51. Substantial changes to plan structure and coverage of FAO's medical insurance plan would be contrary to the harmonization process of existing health insurance schemes of UN organizations, which currently offer similar benefits as shown in Table 8

52. To conclude it must be noted that any changes to plan design and coverage, without placing FAO at a competitive disadvantage, would have a minimal impact on the overall level of ASMC liability. The Organization is still committed to containing the "pay as you go" cost and the ASMC liability through the constant revision and implementation of cost containment measures, which to date have been the most successful drivers in limiting what would have otherwise been an even greater increase in ASMC liability over the past 5 years.

Table 9*

MEDICAL COVERAGE	FAO/IFAD/WFP	IAEA	ILO/ITU	IMO	UN New York International Plan	UN/WMO/HCR	UNOV/UNIDO	UNDP/UN	WIPO	WHO
Physician visits										
Periodic check up % reimbursed	No	€ 546	80%	HIV only	Specific tests	80%	80%		90%	80%
Physician services % reimbursed	80%	80%	80%	80%	80%	80%	80%	80%	90%	80%
Consultants/specialist										
Services % reimbursed	80%	80%	80%	80%	80%	80%	80%	80%	90%	80%
Radiography % reimbursed	80%	80%	80%	80%	80%	80%	80%	80%	90%	80%
Surgery - out patient										
% reimbursed	80%	90%	80%	95%	80%	80%	90%	80%	100%	80%
Surgery - in patient										
% reimbursed	80%	90%	80%	80%	100%	90%	80%	80%	100%	80%
		100% in ward	100% in ward		except doctors fees				90% if private	100% in ward
Prescription drugs										
Prescriptions % reimbursed	80%	80%	80%	80%	80%	80%	80%	80%	90%	80%
Incentive for Generic drug use Y/N	No	No	No	No	No	No	No	No	Yes	No
long-term care available	No	Yes	No	No	No	No	No	No	Yes	No
ELIGIBILITY AND ADMINISTRATION										
Vesting period for full retiree benefits										
Number of years	10	10	10	Data Not available	10	10	10	10	5	10
Minimum age (if applicable)	55	55	55		55	55	50	55	55	55
Transferability vesting rights from other UN org. Yes/No	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Location of treatment										
Restrictions on where treatment may be undertaken Y/N	No	No	No		No	No	No	Yes	Yes	No
Time Limits										
Is there a time limit for claims (Y/N)	Yes	Yes	Yes	Data Not available	Yes	Yes	Yes	Yes	Yes	Yes
If Yes please state time period	2 years	2 years	2 years		2 years	1 year	2 years	1 year	18 months	1 year
COST SHARE										
Basic plan Organization	50%	50%	50%	63%	55%	50%	50%	75%	Data Not available	67%
Staff	50%	50%	50%	37%	45%	50%	50%	25%		33%
Organization	50%	45%	67%	75%	73%	67%	75%	75%	65%	67%
Retiree	50%	55%	33%	25%	27%	33%	25%	25%	35%	33%

***Data to be used for comparative purposes only. Effective dates of data vary from 2004-2010.**

Table 10

	1	2	3	4	5	6	7	8	9	10
	Active staff Covered	Active Staff plus Dependents	Retired staff covered	Retired staff plus dependents	Actuarial valuation of Medical Insurance plan at year end 2010 (USD)	Funding Available (USD)	Unfunded Liability (USD)	Percentage Funded	Unfunded Liability per capita incl. Dependants (USD)	Unfunded Liability Per Capita excl. Dependants. (USD)
FAO	3,478	10,211	4,063	6,615	982,628,000	218,600,000	764,028,000	22.25%	45,408	101,317
WFP	1,650	4,663	471	775	203,700,000	112,800,000	90,900,000	55.38%	16,716	42,857
IAEA	1,440	2,948	652	1,083	244,000,000	0	244,000,000	0.00%	60,531	116,635
UNESCO	2,200	7,627	2,300	5,427	735,600,000	0	735,600,000	0.00%	56,351	163,467
UNIDO	480	1,226	660	880	124,000,000	0	124,000,000	0.00%	58,879	108,772
WHO	10,000	33,000	4,600	7,700	1,365,000,000	450,000,000	915,000,000	32.97%	22,482	62,671
ILO	3,005	7,332	2,143	3,226	564,000,000	40,000,000	524,000,000	7.09%	49,631	101,787
ITU	825	1,900	749	1,096	188,033,000	0	188,033,000	0.00%	62,761	119,462
								AVERAGE	46,594.71	102,120.91

Table 11

Healthcare annual per capita expenditure by Country (figures in USD adjusted for purchasing power parity)	
Country	**Per capita USD**
Austria	3,330.94
Belgium	2,963.78
Canada	3,081.11
Chile	562.02
Czech Republic	1,769.45
Denmark	3,697.90
Estonia	1,049.03
Finland	2,410.28
France	3,100.19
Germany	3,242.31
Hungary	1,053.12
Iceland	2,900.64
Ireland	2,836.09
Israel	1,265.85
Italy	2,442.96
Korea	1,093.26
Luxembourg	4,039.65
Mexico	443.23
New Zealand	2,400.00
Norway	4,501.06
Poland	1,006.06
Slovak Republic	1,369.28
Slovenia	1,893.13
Spain	2,258.58
Sweden	3,032.74
Switzerland	3,071.91
United Kingdom	2,934.59
United States	3,794.85
AVERAGE	**2,412.29**

*OECD Data

Table 12

31 December 2010 Valuation: Modeling Changes in Normal Retirement Age (NRA) and Vesting Service		
Total Defined Benefit Obligation		
Baseline	**$**	**982,628,024**
Scenario 1	$	978,622,246
Change from Baseline		(4,005,778)
Percentage Change from Baseline		-0.4%
Scenario 2	$	932,298,015
Change from Baseline		(50,330,009)
Percentage Change from Baseline		-5.1%
Scenario 3	$	980,700,190
Change from Baseline		(1,927,834)
Percentage Change from Baseline		-0.2%
Scenario 4	$	943,827,828
Change from Baseline		(38,800,196)
Percentage Change from Baseline		-3.9%

Methodology All scenarios use the data and plan rules from the 31 December 2010 valuation.

Baseline - No change

Scenario 1 (Change NRA[8] to 65, No change in early retirement age, no grandfathering[9])

Mandatory retirement age is extended to age 65 with no change in early retirement eligibility.

The current separation rates remain unchanged until age 61.

The new retirement rates at ages 62, 63, and 64 equal the current retirement rates at age 61.

The retirement rates at ages 65 and older remain 100%

Scenario 2 (Change NRA to 65, Change early retirement age to 58, no grandfathering)

Mandatory retirement age is extended to age 65 with early retirement eligibility for the after service medical plan (ASMP) delayed to age 58.

The age to retire under the after service medical plan, with 20+ years of service, while paying the full cost of benefits for some years, increases from age 50 to age 53.

The current retirement rates at ages 55, 56, and 57 (with 10+ years of service) are replaced by the withdrawal rates at those ages.

The new retirement rates at ages 58 to 64 equal the current rates at ages 55 to 61 shifted 3 years--for example, the new age 58 rate equals the current age 55 rate.

The retirement rates at ages 65 and older remain 100%

Scenario 3 (Change NRA to 65, No change in early retirement age, age 55 grandfathering)

There is no change for staff active and over age 55 as of 31 December 2010.

For other staff, the rules and assumptions change as in Scenario 1.

Scenario 4 (Change NRA to 65, Change early retirement age to 58, age 55 grandfathering)

There is no change for staff active and over age 55 as of 31 December 2010.

[8] NRA: Normal Retirement Age

[9] Term used to describe a situation where an old rule(s) continues to apply to some existing situations

For other staff, the rules and assumptions change as in Scenario 2.