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WIPO

A/35/6
ORIGINAL: English
DATE: September 22, 2000

WORLD INTELLECTUAL PROPERTY ORGANIZATION
GENEVA

ASSEMBLIES OF THE MEMBER STATES OF WIPO

Thirty-Fifth Series of Meetings
Geneva, September 25 to October 3, 2000

ADJUSTMENT TO BUDGET PROCESS
POLICY ON RESERVE AND WORKING CAPITAL FUNDS
POLICY ON BUDGET SURPLUS

Memorandum of the Director General

1. The Program and Budget Committee, at its second session from September 20 to 22, 2000, discussed proposals concerning the Adjustment to Budget Process; Policy on Reserve and Working Capital Funds and Policy on Budget Surplus (document WO/PBC/2/2) which is annexed to this document. The views of the Member States represented at the Committee on these proposals, are contained in its report (document WO/PBC/2/6*).

2. The Assemblies of the Member States of WIPO and the Unions administered by WIPO are invited, each as far as it is concerned, to approve the proposals as contained at Annex and the following recommendations made by the Program and Budget Committee:

3. The Chairman noted the position of the Committee on the decision paragraphs in document WO/PBC/2/2:

(a) the wording of paragraph 9 was approved without change;

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* document WO/PBC/2/6 is available for reference

(b) the wording of items (i), (iv), (v) and (vi) of paragraph 49 was approved without change;

(c) the wording of item (ii) of paragraph 49 was approved with the addition, proposed by the Delegation of the United States of America, of the words "for this and subsequent biennia";

(d) the wording of item (iii) of paragraph 49 was approved with the addition, proposed by the Delegation of France, of the words "subject to checking the relevance of these percentages";

(e) a new item (vii) of paragraph 49 was approved, as proposed by the Delegation of the United States of America, with the following wording: "to maintain a clear separation between reserve funds and working capital funds";

(f) the wording of paragraph 71 was approved without change;

(g) the wording of paragraphs 79 and 80 was approved without change.

4. The Chairman also noted the following position of Delegations on paragraph 49 of document WO/PBC/2/2:

(a) with regard to the wording of items (iii) and (v), the Delegations of the United States of America, France and Japan recommended that the Assembly also consider an alternative; it was recommended by those Delegations to delete item (v) and to adopt under item (iii) a PBE factor of 50 per cent for the contribution-financed Unions rather than a PBE factor of 20 per cent as proposed;

(b) with regard to the wording of item (vi), the Delegation of the United States of America recommended that the Assembly also consider the deletion of the item as an alternative.

[Attachment follows]

ATTACHMENT

A. INTRODUCTION

1. This document presents a number of closely related proposals that are seen to transform the budgetary and financial operation of WIPO in a fundamental manner. The current program and budget process includes disconnected decision-making over a lengthy period of time, which limits budget transparency and review. Moreover, some key operations exhibit shortfalls in reserve and working capital funds while WIPO carries forward a high level of liquidity year after year. These issues are addressed in a comprehensive manner, giving due regard to the specific characteristics of WIPO, reflected in its complexity and the dynamics of organizational development. First, it is proposed to streamline the budget process while preserving the two-stage review process recently introduced. Second, it is recommended to align the reserves and working capital arrangement with the financial risk to which each Union is exposed. Finally, it is proposed to link unforeseen budget surplus with the biennial budget process of each Union. The new arrangement will result in major changes during the years to come. The rationalization of the budget process will facilitate decision-making by Member States. The new reserve and working capital arrangement will contribute to a prudent and efficient management of the financial resources. Liquidity will be reduced to an appropriate level and the available funding will be put to full use for the benefit of Member States and the users of the services provided by WIPO.

2. The proposals have been elaborated following comprehensive formal and informal consultations with Member States. At the WIPO General Assembly on March 25 to 27, 1998, the Director General outlined the needs to elaborate a strategic, long-term proposal on the reserve funds and the use of possible budget surpluses. Initial proposals for change were submitted to the Twenty-third Session (September 7 to 15, 1998) of the General Assembly in documents WO/GA/23/2 (Policy on Budget Surplus) and WO/GA/23/3 (Policy on Reserve Funds) and to the First Session (April 26 to 28, 1999) of the Program and Budget Committee in document WO/PBC/1/3 (Policy on Reserve Funds and Surpluses). Moreover, the Director General announced his intention to elaborate proposals for an adjustment of the current budget process during the First Session of the Program and Budget Committee.

3. Advice of Member States received in response to the initial proposal has provided a solid foundation for the Director General to elaborate comprehensive recommendations for approval. Part B of the document describes the new budget process, and Part C, the new reserves and working capital funds arrangement. Part D follows and elaborates the proposal to link the issue of unforeseen budget surplus with the biennial budget process. Finally, Part E of the document outlines the recommended approach according to which the new arrangement is to be implemented.

B. ADJUSTMENT TO BUDGET PROCESS

4. For 2000-2001 biennium, the budget process included a two-stage review of the proposed program and budget. The first stage covered a series of *ad hoc* informal meetings of the Program and Budget Committee for review and comments. This was followed by the preparation of the complete proposed program and budget for review by the regular meeting of the Program and Budget Committee in April of the year prior to the financial period. After

considering the report of the Program and Budget Committee, the proposed program and budget was finally approved by the Assemblies the following September. Prior to this new process, the proposed program and budget had been reviewed only once by the Program and Budget Committee in April and approved by the Assemblies in September.

5. The two-stage review by the Program and Budget Committee is seen to hold considerable advantage over the previous single meeting. Specifically, Member States are better involved in the budget formulation exercise. The major drawback in the current arrangement, however, is the lengthening of the preparatory process whereby it becomes increasingly difficult for the Director General to elaborate meaningful budget proposals prior to the start of the budget period. This becomes more apparent when fully complying with the time limits set for preparation and submission of documentation under the current arrangement. *Illustration A* (see Annex) reflects the current budget review process, but assumes only one informal meeting of the Program and Budget Committee prior to a regular meeting in April. As illustrated, budget preparation would need to commence some 21 months prior to the start of the financial period in order to respect the time limits for preparation and submission of documentation. When examining in detail the current process, it appears that the time between the last meeting of the Program and Budget Committee in April and the meeting of the Assemblies in September presents a gap of four to five months, which is not utilized effectively for budget review. Moreover, due to the early start of the budget process, the document presented to the first informal meeting of the Program and Budget Committee was limited to programmatic information only, which restricted the usefulness of this review exercise for Member States.

6. Building on the improvement in the budget process achieved so far, it is proposed to streamline, shorten and regularize the current two-stage review process. This is achieved by providing for two formal meetings of the Program and Budget Committee. The first regular meeting would be held in April of the year prior to the financial period, as was the case prior to the budget exercise for 1998-1999. Following the review of the proposed program and budget, the Committee could request the Director General, if required, to submit revisions to the proposals. The revised proposals would be prepared by the International Bureau during the summer period and reviewed by a reconvened session of the Program and Budget Committee to be held in September, in the week prior to the meeting of the Assemblies. Prior to the regular sessions of the Program and Budget Committee, informal consultation on budget proposals would be held between Member States and the Director General as was previously the case. According to the proposed adjustments, the program and budget process for the 2002-2003 biennium could be organized as presented in *Illustration B* (see Annex):

- informal consultations between the regional groups, Member States and the Director General from July 2000 to February/March 2001, including *ad hoc* informal meetings of the Program and Budget Committee, if required;

- submission of proposed program and budget by Director General in February/March 2001;

- review of proposed program and budget by first meeting of the Program and Budget Committee in April 2001;

- if requested by first meeting of Program and Budget Committee,

    - submission of proposed revisions to proposed program and budget by Director General in July 2001,

- review of proposed revision to proposed program and budget by reconvened session of the Program and Budget Committee in September 2001, in the week prior to the meeting of the Assemblies;

- approval of program and budget by the Assemblies in September 2001, on the basis of the proposed program and budget and the report of the first meeting of the Program and Budget Committee and, if applicable, the proposed revisions to the proposed program and budget and the report of the reconvened session of the Program and Budget Committee.

7. The proposal for an adjusted budget process preserves the benefit of the current two-stage review process while, at the same time, implementing the process within a reasonable time period. By moving the date of the initial review by Member States closer to the start of the budget period, it is possible for the Director General to submit to the first meeting of the Program and Budget Committee a comprehensive and well-founded proposed program and budget.

8. The Program and Budget Committee is invited to express its views on the adjustment to the budget process.

9. The WIPO General Assembly is invited to approve the adjustment to the budget process, including the holding of a reconvened meeting of the Program and Budget Committee, if requested by the Committee.

C. POLICY ON RESERVE AND WORKING CAPITAL FUNDS

10. WIPO has experienced considerable organizational growth in mandate and level of budget during the recent years. The financial arrangement covering reserve and working capital funds need to be developed alongside such organizational changes in order to ensure that the financial management continues in a prudent and efficient manner.

Current Arrangement: Union Reserve and Working Capital Funds, Separation Reserve

11. As part of the implementation of international agreements and treaties, a complex system of reserves and working capital funds has been established during the life of WIPO and its predecessor organizations. The recent evolution of the present 12 Union reserve and working capital funds and one separation reserve totaling, 77,806,000[1] Swiss francs in 1998-1999, is presented in *Table 1 (see page 5).*

12. As of end-1999, the four Union reserves amount to 56,759,000 Swiss francs. This includes the contribution-financed Unions (Paris, Berne, IPC, Nice, Locarno and Vienna) with 14,869,000 Swiss francs and 16,768,000 Swiss francs for the PCT Union, 24,026,000 Swiss francs for the Madrid Union and 1,096,000 Swiss francs for the Hague Union. According to *WIPO Financial Regulation 8*, the purpose of the reserve funds is to cover any deficits and to receive surpluses of income of the various Unions. By providing a facility to cover

[1] All figures indicated are rounded to the next thousand Swiss francs.

unforeseen deficits, such reserves are available to meet the financial risk of the organization. As shown in *Table 1*, the total amount of Union reserves has increased substantially going from 22,903,000 to 49,491,000 Swiss francs between the 1986-1987 and 1988-1989 biennia. Starting with the 1990-1991 biennium surplus of the PCT, Hague and Madrid Unions were credited to the Special Reserve Fund for Additional Premises and Computerization as described in Part D below. This resulted in much slower increase in the total amount of Union reserves going from 49,491,000 to 56,759,000 Swiss francs for the ten-year period between 1988-1989 and 1998-1999.

13. As of end-1999, the eight Union working capital funds amount to 8,342,000 Swiss francs. This includes the contribution-financed Unions (Paris, Berne, IPC, Nice and Locarno) with five working capital funds of 4,082,000 Swiss francs and 2,000,000 Swiss francs for both the PCT Union and Madrid Union and 260,000 Swiss francs for the Hague Union.

Table 1
Reserve and Working Capital Funds by Union and Separation Reserve
(Thousands of Swiss Francs)

As of December End Biennium	*1986/87*	*1988/89*	*1990/91*	*1992/93*	*1994/95*	*1996/97*	*1998/99*
1. Reserve Funds [a]							
Contribution-Financed Unions							
Paris Union	1,993	2,527	2,080	2,781	3,252	n/a	n/a
Berne Union	1,245	1,577	2,048	2,291	2,508	n/a	n/a
IPC Union	612	1,106	1,438	1,555	2,302	n/a	n/a
Nice Union	598	677	758	832	857	n/a	n/a
Locarno Union	72	107	120	130	138	n/a	n/a
Vienna Union	3	14	16	16	18	n/a	n/a
Total	**4,523**	**6,008**	**6,460**	**7,605**	**9,075**	**14,858**	**14,869**
PCT Union	1,991	21,019	17,019	16,768	16,768	16,768	16,768
Madrid Union	16,260	21,345	24,205	26,246	26,177	24,526	24,026
Hague Union	129	1,119	1,119	1,096	1,096	1,096	1,096
Total, Unions	**22,903**	**49,491**	**48,803**	**51,715**	**53,116**	**57,248**	**56,759**
Separation Reserve	787	1,815	3,489	5,890	9,170	13,588	12,705
Total, 1	**23,690**	**51,306**	**52,292**	**57,605**	**62,286**	**70,836**	**69,464**
2. Working Capital Funds							
Contribution-Financed Unions							
Paris Union	1,593	1,593	1,593	1,593	1,593	1,593	1,593
Berne Union	1,300	1,300	1,300	1,300	1,300	1,300	1,300
IPC Union	333	667	1,000	1,000	1,000	1,000	1,000
Nice Union	160	160	160	160	160	160	160
Locarno Union	29	29	29	29	29	29	29
Total	**3,415**	**3,749**	**4,082**	**4,082**	**4,082**	**4,082**	**4,082**
PCT Union	2,000	2,000	2,000	2,000	2,000	2,000	2,000
Madrid Union	2,000	2,000	2,000	2,000	2,000	2,000	2,000
Hague Union	260	260	260	260	260	260	260
Total, 2	**7,675**	**8,009**	**8,342**	**8,342**	**8,342**	**8,342**	**8,342**
TOTAL	**31,365**	**59,315**	**60,634**	**65,947**	**70,628**	**79,178**	**77,806**

n/a: not available (following the introduction of the Unitary Contribution System since 1996-1997).

[a] In addition, a small reserve fund exists for the Lisbon Union which amounts to 47,000 Swiss francs for 1998-1999.

In accordance with *WIPO Financial Regulation 7*, the working capital funds are to finance expenditure budgeted but not covered by available liquidity. The working capital funds are funded from assessments of Member States that are held in trust by WIPO for the Member States of the respective Unions. As an exception to this arrangement, the working capital fund of the Madrid Union was financed from a transfer from the Madrid Union Reserve Fund in 1979. As shown in *Table 1*, the level of Union working capital funds has essentially remained unchanged during the last ten years.

14. In addition to the Union reserve and working capital funds, a Separation Reserve was established in 1983 to cover the outplacement and separation costs of WIPO staff. The Separation Reserve is funded through a percentage in charge of the gross staff costs and amounted to 12,705,000 Swiss francs as of end-1999.

Shortcoming of the Current Arrangement:
Level of Reserve and Working Capital Funds not Linked to
Financial Risks and Liquidity Requirements

15. Under the current arrangement, reserves are increased or replenished through the transfer of unforeseen surplus of income.[2] This does not ensure that the level of reserves is linked to the risks to which the Union is exposed. In case deficits were generated, the reserve could be insufficient to provide adequate protection. In case surpluses were generated, such transfers might well increase the reserve over-and-above the required level and commit resources unnecessarily.

16. WIPO has experienced considerable overall organizational growth during the recent years. Whereas the budget for the 1986-1987 biennium amounted to 98,846,000 Swiss francs, the budget for 2000-2001 has reached 409,705,000 Swiss francs. In addition, the dynamics of change differed considerably when comparing the various Unions administered by WIPO. While the budget of contribution-financed Unions has declined somewhat, the PCT Union has experienced an average budget growth of 44 per cent per biennium between 1986-1987 and 2000-2001.

17. With organizational growth, the level of financial risk to which WIPO is exposed has increased as well. However, the level of reserves for the PCT, Madrid and Hague Unions has not matched this dynamic despite the generation of considerable surpluses. Surpluses (and interests) in the amount of 313,819,000 Swiss francs were transferred since the 1990-1991 biennium to the Special Reserve Fund for Additional Premises and Computerization as described in detail in Part D below.

18. With regard to the Union working capital funds, the situation is similar to that of Union reserves. The various working capital funds have been established at the time the Unions came in operation. Adjustments would require specific decisions by Member States. In reality, this was not done. Despite the changes in the operation of the Unions and the changes in liquidity requirements, the levels of the working capital funds have remained fixed since 1990-1991.

[2] In addition, as elaborated in paragraph 40 below, Article 8(4) of the Madrid Agreement and Protocol provides a mechanism for the Madrid Union to distribute surpluses to Member States.

PROPOSAL FOR CHANGE:
Reserve and Working Capital Funds (RWC funds)
as Percentage of Estimated Biennial Expenditure (PBE factor)

19. The shortcomings identified above are addressed by proposing an appropriate level of reserve and working capital funds to reflect risk and liquidity concerns specific to each of the Unions. In addition, a mechanism is proposed to adjust the combined level of the reserve and working capital funds to changes that each of the Unions is likely to be faced with in the future. While maintaining the current separation between reserve funds and working capital funds, both are examined jointly in view of the close interrelationship between risk and liquidity concerns.

20. The reserve and working capital funds (RWC funds) are utilized to cover unforeseen deficits as well as to regulate cash flow requirements. This is done to minimize their negative effect on program delivery, to ensure that the Organization can meet its obligations and to provide financial stability. Whereas inadequate provisions expose the Organization to unacceptable financial risks, an excess level of RWC funds is considered inefficient. Moreover, the Director General has a number of options other than the utilization of RWC funds to address possible financial problems. Such measures might include curtailing activities, cost-containment and cost-reduction measures, launch effort to promote the payment of contributions, or defer program implementation. Balance needs to be found between prudent financial management and efficiency concerns.

21. Establishing this balance is not a science but rather a blend of management judgement and practical experience. Central to this is risk management, which involves the identification of a risk, a prudent judgement about its likelihood of occurrence and any resulting financial implications. While the occurrence of certain contingencies may be deemed unlikely, their potential financial impact may be so great as to require adequate protection. When examining such contingencies, full account must be taken to the lack of access of WIPO to the capital markets or the ability to borrow from banks.

22. The issue of financial risk can be elaborated further by distinguishing between income-related and expenditure-related risks. Income-related risks include the non-payment of contributions, lower than anticipated fee-income or exchange rate fluctuations. Expenditure-related risks include, for example, vendor bankruptcy prior to completion of delivery. As it will be demonstrated when examining the requirements for each of the Unions, the most significant risk faced by WIPO is income-related. Essentially, this is the risk that the income which is estimated to be secured during the biennium and which is required to fund the proposed biennial expenditure does not materialize. The proposed biennial expenditure is therefore a good and direct indicator for risk assessment. Hence, it is proposed to express the protection provided by the total amount of RWC funds as a percentage of the estimated biennial expenditure (PBE factor): the higher the PBE factor, the higher the protection. The PBE factor also provides an indication of how long the operation could be funded by drawing exclusively on the RWC funds. For example, a factor of 50 per cent would indicate funding for 12 months and a factor of 25 per cent, funding for six months. In accordance with this approach, *Table 2(see page 8)* provides a presentation of the current RWC funds by Union.

23. As shown in *Table 2*, the PBE factor increased from 17 per cent in 1986-1987 to 49 per cent in 2000-2001 for contribution-financed Unions. For PCT and Madrid Unions, the PBE factor has deteriorated during the last years, with PCT declining from 73 per cent in 1988-1989 to six per cent in 2000-2001. It has been noted that this result is not necessarily a reflection of the financial risks to which each Union is exposed, but the effect of the current policy on handling surpluses and deficits.

Table 2
Reserve and Working Capital Funds by Union and Separation Reserve
(Thousands of Swiss Francs)

As of December End	*1986/87*		*1988/89*		*1990/91*		*1992/93*		*1994/95*		*1996/97*		*1998/99*		*2000/01*	
Biennium	*Amount Sfr*	*PBE %*	*Amount Sfr*	*PBE %*	*Amount Sfr*	*PBE %*	*Amount Sfr*	*PBE %*	*Amount Sfr*	*PBE %*	*Amount Sfr*	*PBE %*	*Amount Sfr*	*PBE %*	*Amount [a] Sfr*	*PBE %*
1. Contribution-Financed Unions																
Reserve Fund																
Paris Union	1,993	8	2,527	10	2,080	8	2,781	10	3,252	13	n/a	n/a	n/a	n/a	n/a	n/a
Berne Union	1,245	10	1,577	13	2,048	16	2,291	18	2,508	21	n/a	n/a	n/a	n/a	n/a	n/a
IPC Union	612	8	1,106	14	1,438	17	1,555	18	2,302	29	n/a	n/a	n/a	n/a	n/a	n/a
Nice Union	598	39	677	43	758	47	832	44	857	51	n/a	n/a	n/a	n/a	n/a	n/a
Locarno Union	72	23	107	34	120	35	130	37	138	43	n/a	n/a	n/a	n/a	n/a	n/a
Vienna Union	3	13	14	58	16	57	16	46	18	55	n/a	n/a	n/a	n/a	n/a	n/a
Total	**4,523**	**10**	**6,008**	**13**	**6,460**	**13**	**7,605**	**15**	**9,075**	**20**	**14,858**	**31**	**14,869**	**33**	**14,869**	**39**
Working Capital Fund																
Paris Union	1,593	6	1,593	6	1,593	6	1,593	6	1,593	7	1,593	n/a	1,593	n/a	1,593	n/a
Berne Union	1,300	11	1,300	11	1,300	10	1,300	10	1,300	11	1,300	n/a	1,300	n/a	1,300	n/a
IPC Union	333	4	667	8	1,000	12	1,000	12	1,000	13	1,000	n/a	1,000	n/a	1,000	n/a
Nice Union	160	10	160	10	160	10	160	8	160	10	160	n/a	160	n/a	160	n/a
Locarno Union	29	9	29	9	29	9	29	8	29	9	29	n/a	29	n/a	29	n/a
Total	**3,415**	**7**	**3,749**	**8**	**4,082**	**8**	**4,082**	**8**	**4,082**	**9**	**4,082**	**9**	**4,082**	**9**	**4,082**	**11**
Total, RWC funds, 1	**7,938**	**17**	**9,757**	**21**	**10,542**	**21**	**11,687**	**23**	**13,157**	**29**	**18,940**	**40**	**18,951**	**42**	**18,951**	**49**
2. PCT Union																
Reserve Fund	1,991	8	21,019	66	17,019	34	16,768	20	16,768	14	16,768	9	16,768	6	16,768	5
Working Capital Fund	2,000	8	2,000	6	2,000	4	2,000	2	2,000	2	2,000	1	2,000	1	2,000	1
Total, RWC funds, 2	**3,991**	**17**	**23,019**	**73**	**19,019**	**37**	**18,768**	**22**	**18,768**	**15**	**18,768**	**10**	**18,768**	**7**	**18,768**	**6**
3. Madrid Union																
Reserve Fund	16,260	70	21,345	92	24,205	81	26,246	63	26,177	54	24,526	43	24,026	41	24,026	44
Working Capital Fund	2,000	9	2,000	9	2,000	7	2,000	5	2,000	4	2,000	4	2,000	3	2,000	4
Total, RWC funds, 3	**18,260**	**79**	**23,345**	**101**	**26,205**	**88**	**28,246**	**68**	**28,177**	**58**	**26,526**	**47**	**26,026**	**45**	**26,026**	**48**
4. Hague Union																
Reserve Fund	129	4	1,119	29	1,119	19	1,096	14	1,096	12	1,096	12	1,096	11	1,096	11
Working Capital Fund	260	9	260	7	260	4	260	3	260	3	260	3	260	3	260	3
Total, RWC funds, 4	**389**	**13**	**1,379**	**36**	**1,379**	**23**	**1,356**	**17**	**1,356**	**14**	**1,356**	**15**	**1,356**	**14**	**1,356**	**14**
5. Separation Reserve	787	1	1,815	2	3,489	3	5,890	3	9,170	4	13,588	4	12,705	3	12,705	3
TOTAL	**31,365**	**32**	**59,315**	**56**	**60,634**	**44**	**65,947**	**35**	**70,628**	**31**	**79,178**	**26**	**77,806**	**20**	**77,806**	**19**

[a] Assumes no change in the level of reserves as compared to the previous biennium
n/a: not available (following the introduction of the Unitary Contribution System since 1996-1997)
PBE: Percentage of Biennial Expenditure; RWC funds: Reserve and Working Capital funds.

24. It is proposed to determine an appropriate PBE factor to each of the Unions with the aim to reflect its risk and liquidity concerns. It is further proposed to determine the level of RWC funds to each of the Unions by applying the PBE factor to the estimated biennial expenditure for the biennium according to the following formula:

Level of RWC funds = estimated biennial expenditure x PBE factor.

25. By selecting estimated biennial expenditure as the reference point, rather than expenditure of past biennia, the level of the RWC funds will be linked to the level of the proposed program and budget. This, in turn, will ensure that the dynamics of change and the related risk and liquidity concerns will be fully reflected in the level of RWC funds.

26. Details on the proposed arrangement – including the PBE factor according to which the total amount of RWC funds is to be established – are elaborated below for the contribution-financed Unions, the PCT Union, the Madrid Union and the Hague Union. A summary of the proposals is provided in *Table 3 (see page 10)* and compared to the current arrangement for the biennium 2000-2001. As shown, it is proposed to decrease the PBE factor from 49 per cent to 20 per cent for contribution-financed Unions and from 48 to 25 per cent for the Madrid Union. The reduction in the reserve for the contribution-financed Unions is linked to the establishment of a provision for past arrears in the amount of 10,390,000 Swiss francs. It is further proposed to increase the PBE factor from 6 to 15 per cent for the PCT Union and from 14 to 15 per cent for the Hague Union. No changes are proposed for the Separation Reserve, since the current level is considered appropriate and the reserve mechanism sufficiently flexible to accommodate future changes. As a result, the total amount of RWC funds would increase from 77,806,000 to 81,312,000 Swiss francs, reflecting an increase from 19 to 20 per cent of the PBE factor for WIPO, in addition to a new provision for past arrears under the contribution-financed Unions.

27. It is proposed that the PBE factor would be approved by the Member States of the Unions concerned and maintained at the same level unless adjusted by a specific decision of those Member States. While maintaining the PBE factor, the level of RWC funds would be adjusted for each of the Unions in accordance with the change in the level of estimated expenditure between biennia. This would be presented as part of the proposed program and budget for the biennium. Whereas any increase in RWC funds or their replenishment would require funding, any decrease would release resources and be reflected in a balanced budget proposal. The details of this mechanism will be further elaborated in Part D (Policy on Budget Surplus).

28. As noted above, the concept of RWC funds is introduced while maintaining the current separation between reserve funds and working capital funds. In addition, the existing arrangement for the working capital funds remains unchanged. Specifically, the assessed contribution through which working capital funds are financed will continue to be held in trust by WIPO for the Member States of the respective Unions. Adjustments in the level of RWC funds will be introduced by amending the level of the reserve funds only, as reflected in *Table 3*. This is seen also to simplify the implementation of the new mechanism. Introducing adjustments also in the level of working capital funds on a biennial basis would be cumbersome and of limited benefit.

Table 3
Current and New Policy on Reserve and Working Capital Funds by Union and Separation Reserve
2000-2001
(Thousands of Swiss Francs)

	Current Policy		*New Policy*		*Difference*
	Amount (Sfr) [a] *A*	*PBE (%)*	*Amount (Sfr) B*	*PBE (%)*	*Amount (Sfr) B-A*
1. Contribution-Financed Unions					
Reserve Fund	14,869	39	3,640	9	(11,229)
Working Capital Fund	4,082	11	4,082	11	-
Total, RWC funds, 1	**18,951**	**49**	**7,722**	**20**	**(11,229)**
2. PCT Union					
Reserve Fund	16,768	5	43,796	14	27,028
Working Capital Fund	2,000	1	2,000	1	-
Total, RWC funds, 2	**18,768**	**6**	**45,796**	**15**	**27,028**
3. Madrid Union					
Reserve Fund	24,026	44	11,657	21	(12,369)
Working Capital Fund	2,000	4	2,000	4	-
Total, RWC funds, 3	**26,026**	**48**	**13,657**	**25**	**(12,369)**
4. Hague Union					
Reserve Fund	1,096	11	1,172	12	76
Working Capital Fund	260	3	260	3	-
Total, RWC funds, 4	**1,356**	**14**	**1,432**	**15**	**76**
5. Separation Reserve	12,705	3	12,705	3	-
TOTAL	**77,806**	**19**	**81,312**	**20**	**3,506**

[a] *Assumes no change in the level of reserves as compared to the previous biennium*
PBE: Percentage of Biennial Expenditure.
RWC funds: Reserve and Working Capital funds.

29. The proposed mechanism for adjusting the RWC funds is considered well suited for a dynamic and complex organization such as WIPO. It captures the dynamics of organizational change characterized by considerable fluctuations between biennia and between the various Unions of WIPO. While remaining simple, the adjustment mechanism ensures that the level of reserves is appropriate – neither excessive nor insufficient – to provide for changes in risk exposure and liquidity requirements. Moreover, the integration of the adjustment mechanism in the budget process provides for full transparency *vis-à-vis* Member States. As indicated in Part E, it is recommended to implement some of the adjustments as of January 1, 2002. With regard to the PCT Union and Madrid Union, it is further recommended to introduce the proposed changes of the RWC funds gradually and in parallel with the reduction in the level of the Special Reserve Fund for Additional Premises and Computerization. Details on the proposed arrangement for the contribution-financed Unions, the PCT Union, the Madrid Union and the Hague Union are presented below.

Contribution-financed Unions

30. The total amount of RWC funds represents 18,951,000 Swiss francs for the 2000-2001 biennium, and has been at about this level since end-1997. With the decrease in the budget of contribution-financed Unions over the last years, the PBE factor has increased from 17 per

cent in 1986-1987 to 49 per cent in 2000-2001. This indicates a relative increase in the RWC funds with the current level amounting to the expenditures of nearly one year of operation.

31. The total amount of 18,951,000 Swiss francs of RWC funds includes the reserve of 14,869,000 Swiss francs and working capital funds of 4,082,000 Swiss francs. This compares to the arrears in contributions amounting to 14,283,000 Swiss francs as of December 31, 1999. Essentially, the arrears amount to the total level of the reserves, leaving a balance of only 586,000 Swiss francs. Growth of arrears is a problem of the past. Of the total arrears of 14,283,000 Swiss francs, an amount of 10,390,000 Swiss francs was accumulated prior to the introduction of the Unitary Contribution System and of four new contribution classes. As of this date, contributions from Member States are generally paid in a regular manner with arrears accumulated since January 1, 1994 amounting to 3,900,000 Swiss francs. As a result, income is more predictable, with total arrears since 1994 corresponding to 10.1 per cent of estimated biennial expenditure for 2000-2001.

32. In the report on the 1998-1999 biennium, the External Auditor of WIPO has commented on the current reserve arrangement of the contribution-financed Unions. It was acknowledged that the current reserve funds are utilized to cover past arrears, rather than future financial risks. In order to de-link those issues, it is recommended by the External Auditor to establish a provision separate from the reserve arrangement to cover all or part of the past arrears. This provision would be reduced in accordance with the payment of past arrears being received. This arrangement would provide financial transparency and allow for the establishment of a lower and appropriate reserve level, reflecting current income risk following the introduction of a Unitary Contribution System in 1994.

33. In accordance with the recommendation of the External Auditor, the Director General proposes to establish a provision of 10,390,000 Swiss francs to cover arrears accumulated prior to 1994. Arrears of 3,900,000 Swiss francs accumulated since 1994 would continue to be covered under the reserve arrangement. Taking into account the pattern of payment of contributions and liquidity requirements, it is proposed to provide a reserve amount of five to six million Swiss francs above the arrears of 3,900,000 Swiss francs accumulated since 1994. As a result, the PBE ratio would be reduced from 49 to 20 per cent and the RWC funds for 2000-2001 from 18,951,000 to 7,722,000 Swiss francs. In total, the new arrangement would amount to 18,112,000 Swiss francs, including RWC funds of 7,722,000 Swiss francs and new provision of 10,390,000 Swiss francs. This reflects a decrease of 839,000 Swiss francs as compared to the current arrangement, which would be accounted for in the context of the budget process for the biennium 2002-2003 as indicated in Part D below.

34. As part of the proposals to adjust the current system, it is recommended to address an inconsistency in the current working capital funds arrangement. With the introduction of the Unitary Contribution System, only a single budget is presented for contribution-financed Unions (Paris, Berne, IPC, Nice, Locarno and Vienna) since 1996-1997. As a result, income and expenses, and therefore deficits or surpluses are identified jointly and not individually for each Union, as was previously the case. Whereas the presentation of the reserve fund was consolidated as of 1996-1997, the working capital funds remain separate in the financial management reporting of WIPO. It is proposed to rectify this prevailing inconsistency by consolidating the presentation of the working capital funds of the contribution-financed Unions in the Financial Management Report. Ownership of working capital funds will remain with the countries that deposited them.

PCT Union

35. The total amount of RWC funds represents 18,768,000 Swiss francs as of December 31, 1999, and it has been at the same level since end-1993. With the considerable increase in the budget of the PCT Union over the last years, the PBE factor has decreased from 73 per cent in 1988-1989 to only six per cent in 2000-2001 with the current level amounting to the funding of some one and a half months of operation. Since 1990-1991, surpluses generated under the PCT Union of 265,060,000 Swiss francs were transferred to the Special Reserve Fund for Additional Premises and Computerization, as outlined below. As a result of this development, the protection provided for RWC funds has deteriorated considerably during the recent years.

36. The PCT Union is exposed to considerable income-related risks, namely unpredictable fluctuations in fee-income as compared to initial estimates. Specifically, the growth rate in PCT applications has fluctuated between 10.3 to 23.1 per cent annually from 1992 to 1999. The level of activity depends upon individual decisions by applicants to apply for international patent protection and those decisions are subject to several factors, including the global economic situation, that are difficult to predict. There is also a currency risk for PCT fee-income since the PCT fees are payable in a number of currencies, and the mechanism for adjusting the level of fees in accordance with exchange rate movements takes some time. Moreover, the reserves should enable WIPO to cover the processing costs of PCT applications over a period of up to 30 months beyond the filing date and to keep the file relating to each international application for at least 30 years. With regard to liquidity, the timing of fees payable is linked to the activities of the International Bureau: PCT fees are received by the International Bureau towards the early part of the process of handling the international application.

37. Whereas it appears difficult to determine an appropriate level of RWC funds for the PCT Union, a number of observations can be made. This fluctuation in the growth of PCT applications has not posed a specific problem in the past, since actual income has consistently exceeded the income estimates after the initial start-up phase. As a result, PCT has generated considerable surpluses and there were no cases of actual usage of the existing reserves. Essentially, this was the result of the unprecedented success of the PCT, not anticipated by Member States or the Secretariat. This success did not only translate in budget increases, but also in considerable reduction of PCT fees since 1997. Based on past experience, it is now possible to improve projections under the PCT Union. Since the budget of the PCT is established by balancing expenditure with anticipated resources, variations in the rate of growth as compared to initial estimates might well result in an unforeseen deficit. The RWC funds would need to accommodate such variation.

38. To give an example, the approved program and budget for 2000-2001 reflects an estimated increase in PCT applications of 22 per cent from 141,000 to 172,000 as compared to 1998-1999. This increase corresponds to 67,500,000 Swiss francs of income for 2000-2001. Should it be the case that PCT applications increased only by 16 per cent as compared to the estimated 22 per cent, the total loss in income would be 18,409,000 Swiss francs, equivalent to the current RWC funds of 18,409,000 Swiss francs. Although lower activities would result in lower expenditures in accordance with the budgetary practice approved by Member States, the PCT Union would run the risk of becoming insolvent in case of major and unforeseen income reductions.

39. The deterioration of the PBE factor of the RWC funds during the recent years does not appear to be consistent with prudent financial management. Based on that assessment it is recommended that the PBE factor be established at 15 per cent, which would cover some three and a half months of operation. This decision would imply an increase in the RWC funds from 18,768,000 to 45,796,000 Swiss francs. This increase would be funded in the context of the budget process, as indicated in Part D below and implemented over a period of several biennia and in parallel to the decrease in the Special Reserve Fund as described in Part E.

Madrid Union

40. The total amount of RWC funds represented 26,026,000 Swiss francs as of December 31, 1999, and it has been at approximately the same level since end-1991. With the increase in the budget of the Madrid Union over the last years, the PBE factor has decreased from 101 per cent in 1988-1989 to 48 per cent in 2000-2001, with the current level amounting to the funding of some 11 ½ months of operation. Since 1990-1991, a total deficit of 2,151,000 Swiss francs was charged to the Reserve Fund. As decided by the Assembly of the Madrid Union, and under Article 8(4) of the Madrid Agreement, surplus is distributed to Member States at a rate of 40 per cent with the remaining 60 per cent being credited to the Special Reserve Fund since 1990-1991. Under this arrangement and since 1989, Member States have been credited 7,957,000 Swiss francs and the Special Reserve Fund 11,938,000 Swiss francs.

41. Due to fewer fluctuations in the level of registrations and renewals, the income-related risk for the Madrid Union is considered to be somewhat lower as compared to the PCT Union. The growth rate in Madrid registrations has fluctuated between a reduction of 1.8 per cent and an increase of 7.8 per cent annually from 1992 to 1999. Similar to the PCT Union, the activities under the Madrid Union are linked to economic situations globally, which are difficult to predict, although the volatility appears to be considerably less. As a result, income predictions have been rather reliable, resulting in small surpluses and deficits. Major changes are expected, however, in the coming years. With the recent accession of Japan and the anticipated accession of the United States of America to the Madrid Protocol, a substantial increase in the level of registration is anticipated. Moreover, with the shortening of the duration of international trademark registration and renewals from 20 years to 10 years as of 1996, it is anticipated that the number of renewals will increase significantly as of 2006 when the new ten-year registrations become due for renewal. In addition to cover possible deficits, the RWC funds should enable the Madrid Union to maintain the international registrations for ten years, whereas the fees are payable only at the beginning of that period. In regard to liquidity, registration and renewal fees are payable by applicants to the International Bureau before the registration or renewal is effected. In addition, funds are available to provide liquidity from complementary and supplementary fees collected by the International Bureau prior to their distribution to the Member States. Liquidity is added from advanced payment of fees and subscriptions to WIPO periodicals. Moreover, the reserve fund of the Madrid Union has been utilized to fund specific projects, such as the Madrid Optical System (MINOS) and the development of ROMARIN (Read-Only Memory of Madrid Actualized Registry Information).

42. Despite its deterioration during the recent years, it appears that the current PBE ratio of the RWC funds is too high. Based on that assessment, it is recommended that the PBE factor be established at 25 per cent, which would cover six months of operation. This decision, if

applied to the biennium 2000-2001, would imply a decrease in the RWC funds from 26,026,000 to 13,657,000 Swiss francs. As proposed for the PCT Union and described in Part E, the decrease in the PBE factor for Madrid would be implemented over a period of several biennia. In this context, it would be prudent to plan for initial expenditure if and when it were decided to introduce Spanish as an additional procedure language in the Madrid system.

Hague Union

43. The total amount of RWC funds represented 1,356,000 Swiss francs as of December 31, 1999, and has been at approximately the same level since end-1989. With the increase in the budget of the Hague Union over the last years, the PBE factor has decreased from 36 per cent in 1988-1989 to 14 per cent in 2000-2001, with the current level amounting to the funding of some three and a half months of operation. Since 1990-1991, surpluses generated under the Hague Union of 3,910,000 million were transferred to the Special Reserve Fund for Additional Premises and Computerization as outlined below.

44. The income-related risk for the Hague Union is considered to be similar to those of the Madrid Union. Particularly, the growth rate in Hague registrations and renewals has fluctuated between 3.1 to 9.6 per cent annually from 1992 to 1999. As a result of the limited volatility, income predictions have been rather reliable, resulting in small surpluses and deficits. International industrial design deposits and renewals made under the Hague system are for a period of five years, while the fees are payable only at the beginning of that period. Reserve funds must be available to maintain the international register for the Hague system for five years in case of a downturn in the level of industrial design deposit activity under the Hague system. With regard to liquidity, the situation for the Hague Union is similar to that of the Madrid Union: registration and renewal fees are payable by applicants to the International Bureau before the registration or renewal is effected. Liquidity is also available to WIPO from the State fees collected by the International Bureau, prior to their distribution to the Member States.

45. Based on that assessment, the current level of RWC funds is considered in the appropriate range and the PBE factor should be established at 15 per cent. This decision would imply an increase in the RWC funds of 76,000 Swiss francs from 1,356,000 Swiss francs to 1,432,000 Swiss francs, which would be funded in the context of the budget process for the biennium 2002-2003 as indicated in Part D below.

Separation Reserve

46. The Separation Reserve amounts to 12,705,000 Swiss francs as of December 31, 1999, and has been established with the 1984-1985 budget. The reserve covers the outplacement and separation costs of WIPO staff, especially if there were to be a need to reduce staff, such as could be associated with a sudden downturn in the level of activity under the PCT, Madrid or Hague systems.

47. The Separation Reserve is unlike other reserve funds, in that it has on-going credits (as a percentage of gross staff costs) and on-going expenditure (when staff separate from service). It has been built up by crediting six per cent of the gross staff costs of all staff engaged since January 1, 1984. In 1998-1999, fund inflow to the reserve was calculated at six per cent of gross staff costs (or 7,957,000 Swiss francs). Actual separation charges for that period

amounted to 8,840,000 Swiss francs. For the 2000-2001 biennium, the accumulation rate will be 1.5 per cent of gross staff costs; that lower rate is expected to approximately balance the amounts credited to the Separation Reserve with the payments made from the Separation Reserve. No changes are proposed for the current Separation Reserve arrangement.

48. The Program and Budget Committee is invited to express its views on the proposed policy on reserve and working capital funds.

49. The WIPO General Assembly or the Assembly of the Union concerned, as the case may be, is invited:

(i) to establish the total level of RWC funds as a percentage of estimated biennial expenditure (PBE factor) for the contribution-financed Unions, the PCT Union, the Madrid Union and the Hague Union;

(ii) to adjust the level of RWC funds according to the approved PBE factor by amending the level of reserve funds only, while preserving the level and ownership arrangement of the working capital funds;

(iii) to approve a PBE factor for the contribution-financed Unions of 20 per cent, the PCT Union of 15 per cent, the Madrid Union of 25 per cent and the Hague Union of 15 per cent;

(iv) to approve the level of the reserve of the respective Union in the context of the proposed program and budget for the financial period, presented as part of the RWC funds;

(v) to approve the establishment of a provision for contribution-financed Unions to cover arrears accumulated prior to 1994 in the amount of 10,390,000 Swiss francs;

(vi) to approve for the contribution-financed Unions the consolidation of the presentation of the working capital funds in the Financial Management Report.

D. POLICY ON BUDGET SURPLUS

50. The budget system of WIPO is founded on the principle of balancing the anticipated availability of resources with anticipated expenditure. On this basis, no surplus is programmed or projected for future biennia. In reality, it is not possible to achieve a perfect balance. When compared to actual results, discrepancies will be recorded. Such discrepancies could be in the form of unforeseen surpluses or deficits.

51. Since 1990-1991, the net surplus of 295,842,000 Swiss francs has been generated, reflecting a surplus of 297,997,000 Swiss francs and a deficit of 2,155,000 Swiss francs. According to *WIPO Financial Regulation 8*, deficits are covered by, and surpluses are paid to, the reserve funds of the various Unions. Accordingly, a total amount of 9,128,000 Swiss francs was received by the reserve funds of the contribution-financed Unions and the Lisbon Union. For the PCT, Madrid and Hague Unions, surpluses generated - in the amount of 280,908,000 Swiss francs - were credited to the Special Reserve Fund for Additional Premises and Computerization as approved by Member States. Before outlining a new policy on the utilization of unforeseen surpluses, the current arrangement with regard to this fund is elaborated below.

Current Arrangement:
Special Reserve Fund for Additional Premises and Computerization

52. The Special Reserve Fund for Additional Premises and Computerization was established by the WIPO Assemblies in 1989 for "constituting a special reserve fund for the additional premises needed to accommodate the increasing number of staff and additional equipment required to handle the ever increasing level of activity of the registration Unions, and for the investments needed in connection with a fuller computerization of registration Unions operations".

53. Since 1990-1991, the Special Reserve Fund received funding amounting to 313,819,000 Swiss francs. This included an amount of 280,908,000 Swiss francs from the PCT Union (265,060,000 Swiss francs), Madrid Union (11,938,000 Swiss francs) and the Hague Union (3,910,000 Swiss francs) as well as 32,911,000 Swiss francs of interest. For the Madrid Union, the amount indicated represents 60 per cent of the surplus generated and the other 40 per cent were distributed to the Madrid Union Member States as described in paragraph 40 above. Of the total Special Reserve Fund, 94.4 per cent were generated under the PCT Union. Whereas WIPO follows a balanced budget approach, the creation of part of the surplus was programmed in view of funding requirements for planned construction and automation projects. This was tied to the growth in the operation of the PCT, Madrid and Hague Unions. Such up-front funding was considered necessary since WIPO does not have access to the capital market. *Table 4 (see page 18)* indicates the increase in amounts credited to the Special Reserve Fund.

54. Of the total 313,819,000 Swiss francs accumulated in the Special Reserve Fund, an amount of 251,635,000 Swiss francs has been committed for specific activities since 1990-1991 by decision of the General Assembly. This leaves a balance of uncommitted surplus funds of 62,184,000 Swiss francs at the end of 1999. It is shown in Table 4 that the largest share of surplus (122,982,000 Swiss francs) was generated during the 1996-1997 biennium, followed by the largest amount of new projects of 206,046,000 Swiss francs, approved in 1998-1999. By the end of 1999, the total level of the Special Reserve Fund amounted to 236,862,000 Swiss francs, reflecting committed and unspent amounts of

174,678,000 Swiss francs (commitment of 251,635,000 Swiss francs minus expenditure of 76,957,000 Swiss francs) and uncommitted funds of 62,184,000 Swiss francs. The total amount of the Special Reserve Fund of 236,862,000 Swiss francs is part of the liquid assets that reached a level of 359,590,000 Swiss francs at the end of 1999. Details on the activities funded from surplus income are indicated in *Table 5 (see page 19)*.

55. As shown in *Table 5*, the type of projects approved varied considerably in terms of size or length of implementation. The important activities are the projects associated with the new building facilities, amounting to 96,054,000 Swiss francs, which will be implemented between 1998 and 2005. The list also includes small projects such as the Madrid System Automation (IMAPS) amounting to 800,000 Swiss francs and covering the replacement of the digital document management and archiving system of the international registry of marks. Whereas resources from the Special Reserve Fund have been approved mainly for specific projects, resources were also provided in 1998-1999 and 2000-2001 to complement the funding of information technology projects programmed under the regular budget for the biennium. With the progressive implementation of the approved activities as indicated in *Table 5*, it is anticipated that this approved funding under the Special Reserve Fund will be spent during the coming years. With such spending expected to reach approximately 70,000,000 Swiss francs in 2000-2001 and 80,000,000 Swiss francs in 2002-2003, the balance of remaining commitments of approved activities are anticipated to decline to 20,000,000 Swiss francs by end of 2003. The relatively high level of the Special Reserve Fund should therefore be considered as being of a transitional nature, due to the large number of major projects currently underway.

Shortcoming of Current Arrangement:
Concern of Resource-Driven Activities, Excess Cash Balances and Parallel Budget Process

56. The current surplus arrangement has attracted a number of concerns by Member States. It has been argued that the level of biennial surplus, in particular for PCT Union, has been unreasonably high in the past. This calls for a re-examination of the current approach of elaborating income estimates.

57. Activities launched under the Special Reserve Fund for Additional Premises and Computerization have been approved by all Member States and are considered of high priority. Nevertheless, it has been argued that rather than being proposed on their own merits, such activities are resource-driven in order to utilize the accumulated resources. Indeed, the last proposal to allocate additional resources from the Special Reserve Fund for a number of new activities was not supported by the Assemblies in September 1998.

58. In addition, the current funding mechanism has resulted in a high level of liquidity considered not being an efficient arrangement. Long-term projects are approved and launched after the full funding has been secured through the accumulation of budget surpluses. This was considered necessary due to the limitation of WIPO to access the capital market. As a result, resources are carried forward year after year and the Special Reserve Fund reached a level of 236,862,000 Swiss francs at the end of 1999. As a result, liquid assets have increased to 359,595,000 Swiss francs, reaching a level considered too high.

Table 4
Special Reserve Fund for Additional Premises and Computerization
(Thousands of Swiss Francs)

End Biennium	*Surplus* [a]			*Commitment*		*Uncommitted*	*Expenditure*		*Commitment*	*Level of*
	Biennium	*% of Income*	*Accumulated A*	*Biennium*	*Accumulated B*	*C=A-B*	*Biennium*	*Accumulated D*	*Unspent E=B-D*	*Reserve Fund F=C+E*
1990/91	34,366	19	34,366	1,000 [b]	1,000	33,366	1,000	1,000	-	33,366
1992/93	50,558	20	84,924	37,590	38,590	46,334	3,300	4,300	34,290	80,624
1994/95	45,579	16	130,503	4,496	43,086	87,417	211	4,511	38,575	125,992
1996/97	122,982	31	253,485	2,503	45,589	207,896	6,788	11,299	34,290	242,186
1998/99	60,334	14	313,819	206,046	251,635	62,184	65,658	76,957	174,678	236,862

[a] *Including interest income of the Special Reserve Fund.*
[b] *Moreover, an amount of 9 million Swiss francs was granted to the Fondation du Centre International de Genève (FCIG) to cover a part of the construction costs of the building at the Administrative Centre of Morillon, which will be repaid, along with one million Swiss francs of interest earned, when WIPO leaves the building.*

Table 5
Special Reserve Fund for Additional Premises and Computerization
(Thousands of Swiss Francs)

Activities	*Expected time of utilization as of 31/12/99*	*Expenditure up to 31/12/99 A*	*Committed from 1/1/00 B*	*Total A+B*
A. Premises				
1. New Building Facilities				
Purchase of Steiner Lot	1998	*13,554*	-	*13,554*
International Architectural Competition	1999-2000	*659*	*841*	*1,500*
Development of Detailed Specifications	2000-2001	-	*2,000*	*2,000*
Construction Work of New Office Building	2001-2004	-	*51,000*	*51,000*
Construction of New Conference Building	2001-2004	-	*15,000*	*15,000*
Construction of Additional Parking Spaces	2001-2004	-	*8,000*	*8,000*
Furniture and Equipment	2004-2005	-	*5,000*	*5,000*
Total 1		14,213	81,841	96,054
2. Renovation of Ex-WMO Building				
Purchase	1999	*34,290*	-	*34,290*
Renovation, Modernization and Extension	1999-2002	*4,919*	*25,481*	*30,400*
Total 2		39,209	25,481	64,690
3. CAM Building [a]	1990	1,000	-	1,000
4. Bodenhausen II	1995-1996	4,496	-	4,496
5. Mezzannine Conversion	1999-2000	343	607	950
6. Study on Premises	1996-1997	317	-	317
Total A. Premises		**59,578**	**107,929**	**167,507**
B. Computerization				
7. PCT Automation	1999-2003	1,471	38,529	40,000
8. Information Technology Projects				
Global Information Network and IP Information Services	1998-1999	*9,622* [b]	-	*9,622*
Information Technology and IP Information Services	2000-2001	-	*28,220*	*28,220*
Total 8		9,622	28,220	37,842
9. Automated Publishing System (DICAPS)	1992-1993	3,300	-	3,300
10. Madrid System Automation (IMAPS)	1998-1999	800	-	800
Total B. Computerization		**15,193**	**66,749**	**81,942**
C. Others				
11. Cooperation WIPO/WTO	1996-1997	2,186	-	2,186
TOTAL		**76,957**	**174,678**	**251,635**

[a] *Moreover, an amount of 9 million Swiss francs was granted to the Fondation du Centre International de Genève (FCIG) to cover a part of the construction costs of the building at the Administrative Centre of Morillon, which will be repaid, along with one million Swiss francs of interest earned, when WIPO leaves the building.*

[b] *Initial budget amounted to 24,948 thousand Swiss francs for the 1998-1999 biennium of which the unspent authority of 15,326 thousand Swiss francs lapsed by the end of 1999.*

59. Finally, the approval of a number of projects from the Special Reserve Fund for Additional Premises and Computerization has established a *de facto* second budget process in parallel and apart from the regular exercise for the biennium budget. In fact, for the 1998-1999 biennium, the projects approved from the Special Reserve Fund of 206,046,000 Swiss francs represents 54.4 per cent of the regular budget for the biennium. This is seen to limit budget transparency whereby the implications of decisions for program and budget are not apparent.

Proposal for Change
Linking Surplus, Deficit and RWC funds with Expanded Concept of Budgetary Balance

60. As noted, surpluses have been accumulated under the PCT, Madrid and Hague Unions for a number of biennia. Since the WIPO budget process is based on presenting a balanced budget, this suggests that the previous assumptions were consistently below-target. Essentially, there can be two reasons for generating surplus: first, lower than budgeted expenditures, second, higher than anticipated income. In the past years, the surplus was a combination of both, although the major share can be clearly attributed to increases in income. When analyzing further the income side, it is noted that surplus can result when, first, the actual number of international applications and/or registrations is higher than that budgeted; second, the actual fee income per application and/or registration is higher than budgeted.

61. Essentially, this was the result of the unprecedented success for the PCT, not anticipated by Member States or the Secretariat. It is now possible to look back on a number of years of experience. Moreover, PCT fees have been reduced considerably in the past: comparing the average fee of 2,800 Swiss francs for 1997 with the budgeted average fee of 1,800 Swiss francs in 2000, the total reduction for this period amounts approximately to one-third since 1997. It appears likely that the levels of surpluses of the past will not materialize in the future. Indeed, whereas the surplus (and interests) for 1996-1997 accounted for 31 per cent of total income, this has declined to 14 per cent in 1998-1999 as shown in *Table 4*. Improvements in projecting the number of international applications and the average fees will be of central concern in the budget exercise for the coming years.

62. When closing the gap between estimated and actual income will be central to the budget exercise, the financial arrangement needs to be prepared for dealing not only with possible surpluses, but also with possible deficits. As outlined above, deficits are covered by an adequate reserve and working capital arrangement. Within the current arrangement, a major deficit under the PCT operation could lead to insolvency. This risk, in turn, might trigger an approach for estimating income which could be considered too cautious. Endorsing the proposals for a new reserve and working capital funds arrangement will establish the foundation based on which realistic income projects can be put forward.

63. Although it is unlikely that the levels of surpluses reached in the past will materialize in the future, a mechanism needs to be established to deal with unforeseen surpluses. One of the key proposals previously put forward in paragraph 29 of document WO/PBC/1/3 suggested that PCT surpluses should be split, with 50 per cent "transferred to the PCT Union Reserve Fund, to be used mainly to finance a PCT fee reduction" and 50 per cent "transferred to the Capital Reserve Fund, from which it could be used to finance important WIPO activities." Subsequent discussion among Member States indicated that such a formula was considered too rigid. This formula was seen to restrict the ability of Member States to decide on matters

of budgetary allocation and the level of fees. Moreover, such a mechanism might well result in the approval of budgetary allocation with limited programmatic justification or in the adjustment of fees with arbitrary long-term implications.

64. Rather than a rigid formula, it is proposed to approve a mechanism by which surplus is linked with the biennial budget process for each Union. By doing so, the issue of surplus is made an integral part of the decision-making process through which the level of budget and the level of fees are determined. Currently, budget proposals balance estimated income with estimated expenditure. It is proposed to achieve in the budget process a balance among a wider range of financial concerns, including accumulated surpluses or deficits and the required level of RWC funds. The new mechanism includes the following steps:

- *Credit surplus and charge deficit to the reserve of the RWC funds:* in accordance with *WIPO Financial Regulation 8.1*, surpluses are paid and deficits are charged to the reserve fund of the respective Union. As a result, the current approach to transfer surplus to the Special Reserve Fund for Additional Premises and Computerization is discontinued.

- *Identify level of RWC funds in accordance with PBE factor as part of budget process*: the level of RWC funds is identified as a percentage (approved PBE factor) of estimated biennial expenditure, as described in Part C of this document. The new level of RWC funds will be gradually established during the biennium along with the implementation of the approved budget.

- *Link excess or shortfall in RWC funds to budget process of each Union:* any RWC resources in excess of the established level of RWC funds are available for funding the proposed biennial expenditure; any shortfall would constitute a resource requirement. For the Madrid Union, this is implemented subject to Article 8(4) of the Madrid Agreement and Protocol. Resources in excess of the RWC funds are likely to materialize in case a major surplus becomes available; a shortfall might result in case a budget deficit is incurred.

- *Balance estimated resource availability and requirement for the biennium*: the new budget balance includes a wider range of financial concerns. The estimated availability of resources covers the estimated biennial income as is currently the case and, if applicable, excess in RWC funds; the estimated requirements of resources covers the estimated biennial expenditure as is currently the case and, if applicable, shortfall in RWC funds. This expanded concept of budgetary balance can be summarized by the following equation:

Estimated biennial income
<u>+Excess in RWC funds, if applicable</u>
= estimated resource availability

equals

Proposed biennial expenditure
<u>+Shortfall in RWC funds, if applicable</u>
= estimated resource requirement

65. The balance between resource availability and requirement will be presented in the context of a four-year financial plan annexed to the budget document. This will provide an opportunity to demonstrate that decisions proposed for the budget period can be sustained during a longer-term period. Such decisions may include long-term commitments or fee reductions which have major ongoing implications.

66. As outlined above, the issue of surplus, deficit and the level of RWC funds are accounted for in an expanded concept of budgetary balance. With the focus on unforeseen surpluses and deficits, the flow of resources is demonstrated in *Illustration C* (see Annex) by using financial data as an example only. As can be seen, the total amount of surplus (or deficit) anticipated by mid-biennium would be fully accounted for in the budget process for the subsequent biennium. As a result, the balance of accumulated surplus is likely to decline in the coming years putting the resources to use, either for budget funding or for fee reduction. This is done in a transparent manner. When presented as part of a consolidated budget, activities are justified in reference to the total work program. This excludes possible concern of resource-driven support associated with *ad hoc* initiatives. Moreover, the integration of surplus resources ensures that the budget proposal is presented in a unified manner and the parallel and disconnected process of regular budget and Special Reserve Fund projects is discontinued.

67. The new surplus policy does not impact on the budgetary arrangement for projects currently funded under the Special Reserve Fund for Additional Premises and Computerization. With those projects being implemented, the high level of the Special Reserve Fund will decrease considerably during the coming years as noted above. As noted above, surpluses would be transferred to the reserve of each Union and the current arrangement of crediting the surplus of the PCT, Madrid and Hague Unions to the Special Reserve Fund would be discontinued. This would also apply to the interest earned under the Special Reserve Fund. Such interest would be credited to the reserve of the respective Union in accordance with its share of funding of the Special Reserve Fund. The Special Reserve Fund would therefore cover only the budgetary provisions of projects approved by Member States.

68. The new surplus policy also implies a more efficient approach to the launch of new long-term projects. Rather than providing full funding up front as is currently the case under the Special Reserve Fund arrangement, such projects would be integrated, justified and funded as part of the biennial budget process. This would be done by outlining the biennial programmatic and budgetary proposals, but also by elaborating the long-term implications in the context of the four-year financial plan annexed to the budget document. The biennial approach to the funding of long-term projects would discontinue the need to maintain a high level of liquid assets over a long period of time.

69. The new surplus policy is seen to contribute to a rationalization of the budget process as outlined above and would be applied in accordance with its biennial cycle. This new policy would not limit, however, the prerogative of the Director General to propose, and of Member States to approve, projects funded from unforeseen surplus resources or changes in the level of registration fees during mid-biennium and outside the regular budget process. Such decisions, however, would be regarded as an exception to the new policy and justified accordingly. This is the case for the biennium 2000-2001, whereby proposals are put forward during mid-biennium to increase the budgets of two projects funded from the Special Reserve Fund for Additional Premises and Computerization.

70. The Program and Budget Committee is invited to express its views on the proposed policy on reserve and working capital funds.

71. The WIPO General Assembly or the Assembly of the Union concerned, as the case may be, is invited:

(i) to approve to discontinue the transfer of surpluses of the PCT, Madrid and Hague Unions to the Special Reserve Fund for Additional Premises and Computerization and thereby revert to having such surpluses paid to the reserve fund of the respective Union in accordance with WIPO Financial Regulation 8.1;

(ii) to approve that excess or shortfall in resources as compared to the established level of RWC funds are accounted for in the biennial process of each Union, subject, as concerns the Madrid Union, to Article 8(4) of the Madrid Agreement and Protocol;

(iii) to note that the policy on budget surplus does not restrict the prerogative of the Director General to propose for approval by the WIPO General Assembly or the Assembly of the Union concerned, as the case may be, project activities funded from available surplus.

E. NEW BUDGET PROCESS AND POLICY ON RESERVE, WORKING CAPITAL FUNDS AND SURPLUS: IMPLEMENTATION APPROACH

72. It is proposed to implement the new budget process for the review and approval of the program and budget 2002-2003. This would imply releasing the proposed program and budget 2002-2003 in February/March 2001, having the first meeting of the Program and Budget Committee in April 2001 and a possible reconvened session of the Program and Budget Committee in September 2001, followed by the ordinary session of the Assemblies also in September 2001.

73. It is also proposed that the new policy on reserves, working capital funds and surplus be implemented in the context of the budget exercise for the biennium 2002-2003. This includes that uncommitted surplus resources from 1998-1999 are accounted for in the new budget process. At end-1999, such uncommitted surplus amounted to 62,184,000 Swiss francs under

the Special Reserve Fund for Additional Premises and Computerization (see *Table 4*, column C). The Director General will submit proposals to the WIPO General Assembly in September 2000 for adjusting project budgets funded under the Special Reserve Fund. The amount of uncommitted surplus from the biennium 1998-1999 available for the budget process 2002-2003 will therefore be determined following decisions of the WIPO General Assembly on the proposed budget revisions.

74. As part of introducing the new policies in the budget exercise 2002-2003, the level of RWC funds will be proposed in accordance with the approved PBE factor. When compared to the biennium 2000-2001, the new policy would have limited budgetary implications for the contribution-financed Unions and the Hague Union. For the contribution-financed Unions, this would imply lower resource requirements of 839,000 Swiss francs, reflecting a PBE factor of 20 per cent (reduction in the reserve by 11,229,000 Swiss francs) and the new provision of 10,390,000 Swiss francs for past arrears. For the Hague Union this would imply an increase in resource requirements by 76,000 Swiss francs due to the introduction of a PBE factor of 15 per cent. It is therefore recommended to fully implement the new policy for the contribution-financed Unions and the Hague Union in the proposed budget 2002-2003.

75. In contrast to the immediate implementation of the proposals for the contribution-financed Unions and the Hague Union, it is recommended to implement the new policy for the Madrid and PCT Union in a gradual manner, starting with the biennium 2002-2003. This will ensure that the major budgetary implications resulting from this new policy will not lead to a disruption of the budget process for the Madrid and PCT Union and are justified in the context of the overall financial situation of WIPO.

76. With regard to the Madrid Union, the recommended PBE factor is 25 per cent. On the basis of the 2000-2001 level of estimated expenditure, such an adjustment would result in a decrease of the RWC funds by 12,369,000 Swiss francs, equivalent to 22.6 per cent of the budget 2000-2001. Decreases in the reserve funds are linked to the budget process as outlined in Part D. In order to ensure that the budgetary implications resulting from such a drastic reduction are sustainable, it is proposed to introduce the PBE factor of 25 per cent in the level of RWC funds for the Madrid Union in a gradual manner and during the coming three biennia. As a first step and in order to facilitate this adjustment process, it is further proposed to distribute 100 per cent of any surplus that may be accumulated during the biennium 2000-2001 to Member States under Article 8(4) of the Madrid Agreement and Protocol. This compares to 40 per cent as was previously the case. Corresponding proposals for subsequent biennia will be presented in the context of the respective budget process.

77. With regard to the PCT Union, the recommended PBE factor is 15 per cent. On the basis of the 2000-2001 level of estimated expenditure, such an adjustment will require an increase in the RWC funds by 27,028,000 Swiss francs equivalent to 8.9 per cent of the budget for the PCT Union for 2000-2001. If accounted for in one budget period, it appears difficult to accommodate such an increase. Moreover, when considering the overall financial situation of WIPO, it appears justifiable to delay an increase of reserve funds. This is possible since the Special Reserve Fund for Additional Premises and Computerization stands at 236,862,000 Swiss francs at the end of 1999. With the implementation of the approved projects funded under the Special Reserve Fund during the coming biennia, the Fund and the high level of liquidity will decrease. It is therefore proposed to introduce the PBE factor of 15 per cent for the PCT Union in a gradual manner and linked to the decrease of the Special Reserve Fund. Specifically, for the 2002-2003 biennium, a PBE factor of approximately

10 per cent could be applied, with the remaining increase being introduced during the 2004-2005 and 2006-2007 biennia. This approach would avoid establishing excessive reserves in view of the current overall financial situation of WIPO and thereby maximize the available funding which will be put to full use for the benefit of Member States and the users of the services provided by WIPO.

78. The Program and Budget Committee is invited to express its views on the proposed implementation approach.

79. The WIPO General Assembly or the Assembly of the Union concerned, as the case may be, is invited to approve the implementation approach.

80. The Assembly of the Madrid Union is invited to approve that 100 per cent of any surplus accumulated during the biennium 2000-2001 is to be distributed to Member States under Article 8(4) of the Madrid Agreement and Protocol.

[Annex follows]

Illustration A

Current process of budget preparation, review and approval 2002-2003

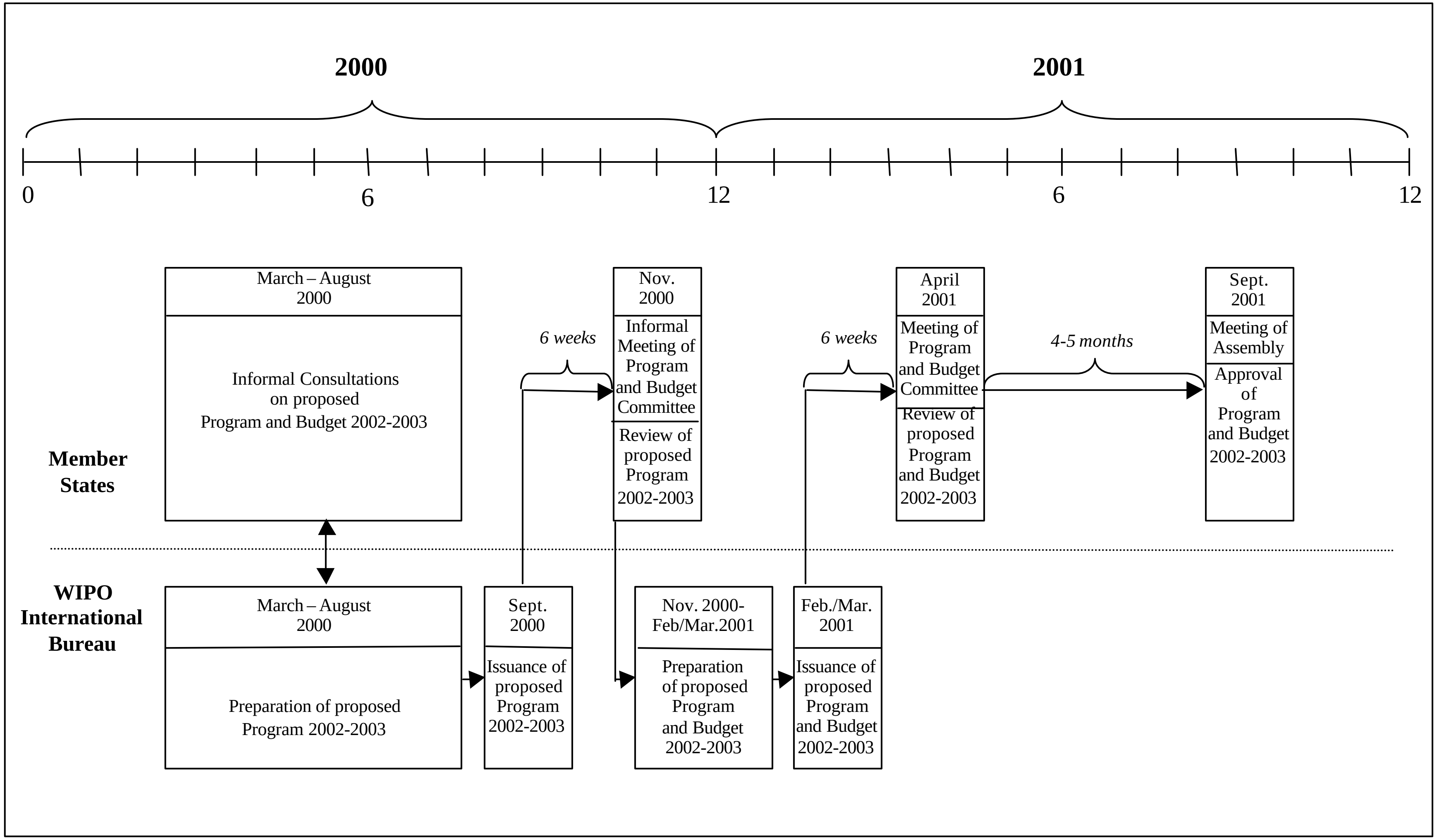


Illustration B

New process of budget preparation, review and approval 2002-2003

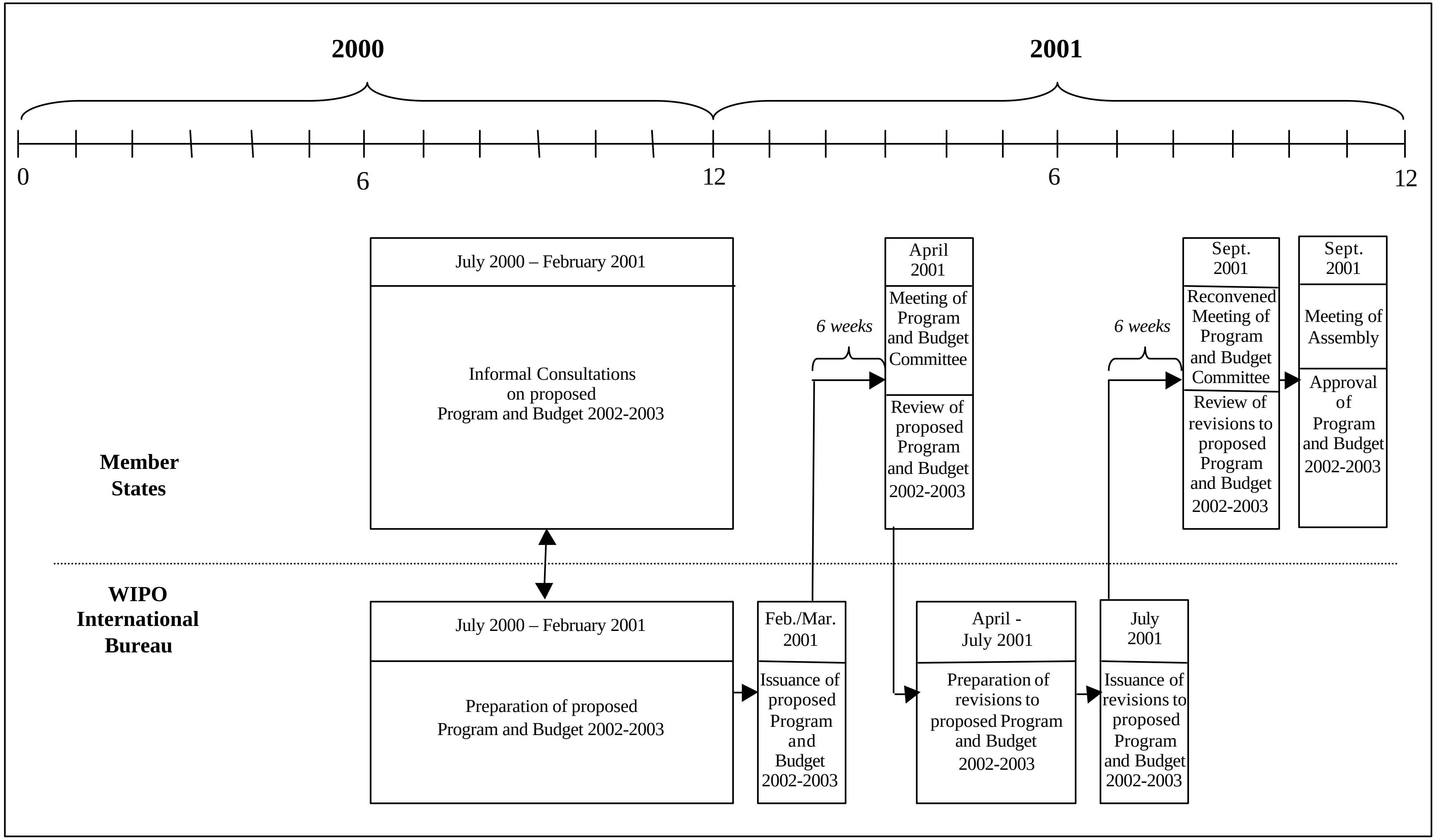
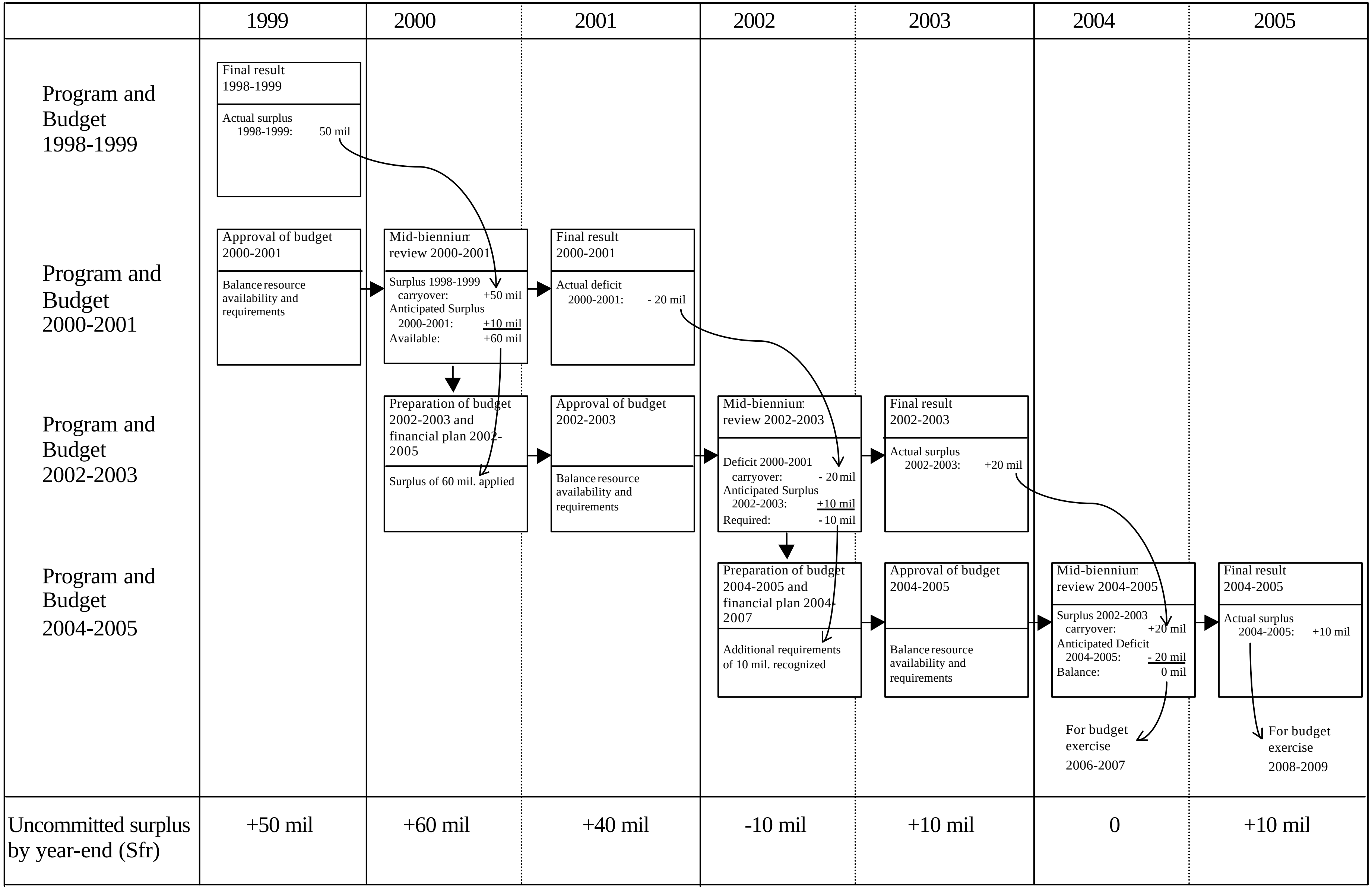


Illustration C

Integration of unforseen surpluses and deficits in the budget process

(Financial data in Swiss francs and provided as examples only)



[End of Annex and of document]