E

WIPO
WORLD
INTELLECTUAL PROPERTY
ORGANIZATION

WO/PBC/19/23
ORIGINAL: ENGLISH
DATE: JUNE 20, 2012

Program and Budget Committee

Nineteenth Session
Geneva, September 10 to 14, 2012

LONG-TERM FINANCING OF AFTER-SERVICE HEALTH INSURANCE (ASHI) IN WIPO

Document prepared by the Secretariat

EXECUTIVE SUMMARY

1. The adoption of International Public Sector Accounting Standards (IPSAS) by WIPO has resulted in a requirement that the Organization recognize its total liability for employee benefit entitlements payable to active and former officials in its financial statements.

2. The most significant element within the employee benefit liability relates to After-Service Health Insurance (ASHI). This liability has increased by 89 per cent over the past six years and reached 103.4 million Swiss francs at the end of 2011.

3. In the 2010/11 and the previous biennia, the budget included a charge of six per cent of payroll costs. This approach was not sufficient to fund this liability.

4. An increase in the amount of the liability has significant consequences for WIPO since, under IPSAS, any increase in the liability involves recognition, in the financial statements, of a decrease in WIPO's reserves. The Secretariat believes that a proper solution to finance this liability should be found.

5. Four options are evaluated in this document and one of them is proposed as the best course of action to solve the problem and finance the liability.

6. IPSAS-25 provides a way of mitigating the impact of changes in the ASHI liability for organizations that finance part of the ASHI liability, in whole or in part, by means of setting up a separate entity.

7. With a one-time transfer to a new, separate entity, of 50 million Swiss francs taken from the Organization's available cash and a continued annual funding of 6.5 per cent of payroll costs, WIPO could fully fund the ASHI liability in about 12 years. This 50 million cash transfer from WIPO's balance sheet to the separate entity balance sheet would not modify the financial situation of the Organization nor the amount of the WIPO reserve funds as the said cash transfer would be counterbalanced by the corresponding transfer of 50 million of WIPO's ASHI liability to the separate entity.

BACKGROUND

8. The adoption of IPSAS by WIPO has resulted in a requirement that the Organization recognize in its financial statements its total liability for employee benefit entitlements payable to active and former officials. At December 31, 2011, these liabilities totaled 131.7 million Swiss francs. Of this amount, 103.4 million Swiss francs (or 78.5 per cent) represented the ASHI liability for former staff members and survivors and their dependents, with the balance representing liabilities for repatriation grants and travel, accumulated unpaid annual leave, WIPO's share of the liabilities of the WIPO Closed Pension Fund (CROMPI), overtime pay and education grants.

9. For WIPO, as for most of the organizations of the UN system, the most significant element within the employee benefit liability relates to ASHI. This liability has increased by 89 per cent over the past six years as follows:

Year	**Defined Benefit Liability**	**Increase**	**% Increase**
2005	54'714'000		
2007	64'625'000	9'911'000	18.11%
2009	82'603'476	17'978'476	27.82%
2010	95'932'119	13'328'643	16.14%
2011	103'364'650	7'432'531	7.75%
2005 to 2011		48'650'650	88.92%

Note – studies prior to 2010 were biennial

This liability is calculated by WIPO's actuary (Mercer) and reflects the total future costs of WIPO's share of health insurance premiums for both existing WIPO retirees and the projected number of active WIPO staff that will retire in the future in either the United Nations Joint Staff Pension Fund (UNJSPF) or CROMPI. Beginning in 2009, the calculation has been determined in accordance with the requirements of IPSAS-25 - Employee Benefits, and is based on assumptions agreed with the actuary and accepted by the External Auditor.

10. At WIPO, ASHI coverage is provided by an insurance carrier (Van Breda). Retirees are eligible for the same insurance coverage as active staff. All former staff members that are receiving pensions from either the UNJSPF or the CROMPI are eligible to continue their medical insurance coverage after retirement including coverage for dependent spouses and children. At December 31, 2011, 302 former staff members, and 205 dependents of retirees were covered by the WIPO insurance policy.

I. CURRENT ASHI CHARGES IN WIPO

11. Retired staff members make a contribution toward their insurance equal to 35 per cent of the premium established by the insurance carrier. WIPO covers the remaining 65 per cent of the premium. For 2011 and 2010, the monthly premiums paid were as follows:

Per covered adult	552 Swiss francs
Per covered child	245 Swiss francs

12. In 2010, the total WIPO share was 1.8 million Swiss francs and in 2011, 1.9 million Swiss francs. For the 2010/11 biennium, the cost was charged to the budget. Beginning with the 2012/13 biennium, the payments to the insurance carrier will be charged to the provision for the ASHI liability calculated by the WIPO's actuary.

II. HOW ASHI IS CURRENTLY FUNDED IN WIPO

13. In the 2010/11 and the previous biennia, the budget included a charge of six per cent of payroll costs, which was utilized to fund cash payments made to staff for separation benefits, including payments of unused annual leave, repatriation grants and repatriation travel. Any remaining balance was accumulated as a reserve on WIPO's balance sheet to finance future liabilities for these benefits. At the end of 2009, 46.0 million Swiss francs had been accumulated in WIPO's reserves. As part of the adjustments required for the implementation of IPSAS, this amount was utilized to offset the requirement to recognize on the balance sheet the full liability for ASHI. This reduced the negative impact of the IPSAS adjustments. Several other UN agencies that had not set aside any funding experienced the full impact of the IPSAS adjustments.

14. In 2010, 9.2 million Swiss francs and in 2011, 9.5 million Swiss francs were made available as a result of the change of six per cent of payroll costs to reduce the IPSAS adjustment required to recognize the ASHI liability. Had these amounts not been available, the IPSAS adjustments for the 2010/11 biennium would have been higher.

15. In the 2012/13 budget, the 6 per cent of payroll costs included in the budget had to be reduced to 2 per cent due to financial constraints. The two per cent charge will be used to cover the costs of the payment of separation benefits to departing staff such as unused accumulated leave, repatriation grants and repatriation travel expense. Any unused portion will be available to reduce the ASHI liability. However, it is unlikely that any significant amount will remain after these payments are made. This reduction, along with the removal from the budget of funds to finance the current expense of retiree health insurance discussed in section I above will become part of the IPSAS adjustments. The estimated IPSAS adjustments for the 2012/13 biennium required to finance the increase in ASHI liability are 19.8 million Swiss francs.

III. WHAT ARE THE NEW IPSAS REQUIREMENTS AND THEIR CONSEQUENCES?

16. Under IPSAS (IPSAS-25, paragraphs 59-146), organizations producing IPSAS conforming financial statements must recognize the full liability at the end of each financial year for employee benefits including defined benefit plans. ASHI is a defined benefit plan since WIPO's obligation is to provide agreed benefits (those covered by the Staff Regulations and Rules) to current and former employees and any risk that benefits will cost more than the revenue derived from contributions falls on WIPO.

17. Under IPSAS-25, the ASHI liability of the Organization must be recognized on an entity's balance sheet (Statement of Financial Position). WIPO initially recognized this liability as part of the opening IPSAS adjustments at January 1, 2010. The total liability recognized in 2009 was 82.6 million Swiss francs. By the end of 2011, the liability had increased to 103.4 million Swiss francs, an increase of 20.8 million Swiss francs (or 25.2 per cent).

18. Under IPSAS the calculation of the ASHI liability is based on the Projected Unit Credit actuarial methodology, which requires recognition each year of the change in the total of a defined benefit obligation resulting from:

(a) Current service cost–defined in IPSAS as the increase in the present value of the defined benefit obligation resulting from employee service in the current period. This is the impact resulting from the increase in age of current staff, retired staff and their dependents; the number of persons retiring in the current year; and new hires and separation other than retirement during the current year.

(b) Interest cost–defined in IPSAS as the increase during a period in the present value of a defined benefit obligation that arises because the benefits are one period closer to settlement. This is the impact resulting from the fact that each member of the active staff is one year closer to reaching the age of eligibility for ASHI on retirement.

(c) Actuarial gains and losses: In addition to these costs, the ASHI liability is impacted by other factors taken into consideration by the actuary. These include the projected increase in health care costs (sickness premium increase) and changes in mortality rates based upon rates agreed with the actuary and the External Auditor. These rates are then utilized by the actuary to project the total amount of the liability.

(i) Sickness premium increase: At WIPO, the projected increase in health care costs is calculated based upon the average increase in health care costs in Geneva during the previous 3-5 years. For 2009 the rate utilized was 2.1 per cent, 2.5 per cent in 2010 and for 2011 3.0 per cent, decreasing to 2.5 per cent after five years and to 2.0 per cent after 15 years. Each 1 per cent increase in health care costs results in an increase of 11.8 million Swiss francs in WIPO's total liability. As health care costs in Geneva have increased at a faster rate in recent years, the impact of this factor on the liability will also increase.

(ii) Mortality rates: WIPO's actuary utilizes mortality tables computed by the Swiss Government which are updated every five years. The latest rates, published in 2010 have been utilized for the calculation of the 2011 ASHI liability. During the five year period between updates, the average age for men increased from 82.9 years to 83.9 years, and for women from 86.0 years to 86.4 years. The improvement in life expectancy has a significant impact on the ASHI liability as it is used to determine the number of months each current and future retiree and dependent will be expected to benefit from ASHI.

(iii) Discount rates: In addition, in order to take into consideration the impact of inflation on the liability which will be paid over many future years, the actuary discounts the liability to reflect its value at the date of the financial statements (present value). This discount is based on the rate of high grade corporate bonds in Swiss francs available at the reporting date. If the discount rate increases, the present value decreases, and if the rate decreases the present value increases. For 2009 a discount rate of 3.25 per cent was utilized, for 2010 a rate of 3.00 per cent and for 2011 a rate of 2.75 per cent.

IV. OPTIONS AVAILABLE FOR THE FUTURE: TRYING TO FUND THE ASHI LIABILITY IN THE BEST POSSIBLE WAY.

19. An increase in the amount of the liability has serious consequences for WIPO as, under IPSAS, any increase in the liability involves the recognition, in the financial statements, of a decrease in WIPO's reserves. WIPO could consider several options in this situation:

IV.1 Option 1: Continue the present approach

20. As indicated, for the 2012/13 biennium the funds available in the budget to finance the ASHI liability have been reduced significantly due to the change in the charge for separation benefits from 6 to 2 percent. This arrangement has been decided on solely due to specific financial constraints anticipated for this biennium. However, should the present approach continue to be adopted, the impact of increases in the ASHI liability would be financed as an IPSAS adjustment reducing the net result from operations and consequently the reserves reflected on the financial statements. The annual expense related to the change in ASHI liability will continue to increase as more employees become eligible for ASHI, the reserves will diminish and, consequently, the ASHI liability will never be funded.

IV.2 Option 2: Provide sufficient "budgetary" funding for the ASHI liability

21. An alternative would be to finance the ASHI liability through budgetary funding. By restoring the payroll charge to its previous 6 per cent rate, the additional funds would be available to finance the annual expense for current service cost, interest cost, the amortization of actuarial gain and loss and the benefits payable to retirees. This solution would only freeze the ASHI liability near to its current level for the immediate future, unless there were significant changes in demographics due, for example, to a new voluntary redundancy program. Two United Nations organizations have adopted similar approaches.

22. If the payroll charge could be increased to 9.0 per cent, sufficient funds would be available to begin to reduce the ASHI liability provision maintained on WIPO's balance sheet. It is estimated that the additional funding would be sufficient to reduce the provision required to zero in approximately 30 years (assuming there are no drastic changes in the discount rate or medical cost increase rate which is unlikely to be the case over such a long period of time). Under this approach the utilization of the funds would not be specified and the Assemblies could choose to utilize the funding for other purposes, which would unfortunately signify that the long-term financing of this entity cannot be guaranteed.

IV.3 Option 3: Provide "separate" funding for the ASHI liability

23. The WIPO actuary has calculated that by imposing a separate 6.5 per cent charge of payroll costs for ASHI, maintaining the funds produced by such a charge in a separate ASHI fund and investing the funds in long-term Swiss franc bonds, this would enable the Organization to fully fund its ASHI liability over a period of 19 years. This analysis is based upon certain assumptions including a market yield of 2.0 per cent on the bonds. If bond yields increase in the future, the period required to fully finance the liability would decrease. If bond yields decrease in the future, the period required to fully finance the liability would increase, however, this is felt to be unlikely given the very low current bond yields.

24. Similar approaches have been adopted by the International Fund for Agricultural Development (IFAD), Pan American Health Organization (PAHO) and the World Health Organization (WHO), International Labour Organization (ILO) and International

Telecommunications Union (ITU) in their joint plan and the International Civil Aviation Organization (ICAO). Each of the organizations has established a separate fund to accumulate resources to contribute toward the long-term financing of their ASHI liabilities financed either from one time transfers from accumulated surpluses, with funds accumulated from the excess of payroll charges over current costs or both. These funds are treated as separate reserves and are generally separately invested in long-term bonds that reflect the average working life of active employees before retirement. By investing the funds separately in long-term bonds with maturities related to the organization's liability, the organizations have made a long-term commitment toward financing of these liabilities.

25. These funds are established by legislation adopted by each entity or by the regulations of their Staff Health Insurance funds. All of the earnings on the investments held in the separate ASHI reserve funds are retained in the funds and reinvested, helping to offset the impact of the growth in ASHI liabilities.

IV.4 Option 4: Establish an independent entity to manage the ASHI liability

26. IPSAS-25 provides a way of mitigating the impact of changes in the ASHI liability for organizations that finance part of the ASHI liability, in whole or in part, by means of setting up a separate entity. This entity could be initially financed by a transfer of cash resources that would be held by the entity along with annual transfers based upon the resources that could be made available from WIPO's budget through a payroll charge. The initial transfer would not impact on WIPO's balance sheet since its assets (cash) would be reduced by the amount transferred to the new entity along with an offsetting equal reduction in the amount of WIPO's ASHI liability that would be assumed by the entity.

27. The annual transfers made to the entity would be utilized to pay the current year's cost of WIPO's share of the health insurance premiums for retirees and dependents. Any balance remaining along with the funds from the initial transfer would be invested in conservative investments for the long-term, in accordance with WIPO's approved Investment Policy. The total amount held by the entity at the end of each year including accumulated investment earnings would reduce WIPO's ASHI liability.

28. In addition, by providing funding through such a separate entity, WIPO's liability would decrease significantly, not just by the amount made immediately available but also by the amount of projected revenue (as calculated by the actuary) that would be generated through interest earnings if the funds were invested. In addition, the annual volatility would also be reduced since increases in the ASHI liability caused by changes in demographics such as age of WIPO staff, changes in actuarial mortality tables, etc. would be offset by the growth of revenue from investments.

> **Option 4(a)**: A separate entity could be created under Swiss law. In such a case, the entity would have a specific name (for instance, the WIPO ASHI fund), and a separate governance structure from that of WIPO. The entity would be independent, and funds given to the entity could not revert to WIPO unless the total amount held by the entity exceeded the total ASHI liability. Even though the entity would be separate, its accounts and investments could be managed by WIPO's Finance Services.

> **Option 4(b)**: An alternative would be to transfer the funds to a separate entity created under international law by WIPO. In such a case, the entity would have a specific name (for instance, the WIPO ASHI fund) and a separate governance structure from that of WIPO. The entity would be independent and funds given to the entity would remain within it and would only be returned to WIPO if the total amount held by the entity were to

exceed the total ASHI liability. Even though the entity would be separate, its accounts and investments could be managed by WIPO Finance Services, thus involving a minimum of supplementary administrative costs.

CONCLUSION

29. It is considered that establishing a separate entity is more efficient and less heavy in budgetary terms. The Organization would not recommend that this entity be placed under Swiss law in order to avoid being subject to potential variations in Swiss legislation, which may not be adapted to the specificities of an international organization with its mode of evolution and different kind of target population. For these reasons, the Organization recommends Option 4(b).

30. Option 4(b) requires approval by the Member States as it entails the setting up of a separate entity. This entity could have its own independent governance under the supervision of the Director General. This entity would report financially to the Member States on a yearly basis in the same way as WIPO. Its aim would be to finance the ASHI liability within an approximate 12 to 15-year time frame.

31. Using this approach, with a one-time transfer to the new entity of 50 million Swiss francs taken from the Organization's available cash and a continued annual funding of 6.5 per cent of payroll costs, WIPO could fully fund the ASHI liability in about 12 years. This 50 million cash transfer from WIPO's balance sheet to the separate entity balance sheet would not modify the financial situation of the Organization nor the amount of the WIPO reserve funds as the said cash transfer would be counterbalanced by the corresponding transfer of 50 million of WIPO's ASHI liability to the separate entity. Adoption of this approach would enable WIPO, over the 12 year period indicated, to eliminate the annual drain on the reserves necessary to finance the ASHI liability.

32. There is merit in tackling the issue of how to fund this ASHI liability now, as a delay would lead to an increase in the liability and the corresponding funding would inevitably need to be found.

33. The Program and Budget Committee is invited to:

(i) examine the options for the long-term financing of ASHI presented in this document; and

(ii) recommend to the Assemblies of the WIPO Member States the implementation of option 4(b) described in this document.

[Annex follows]

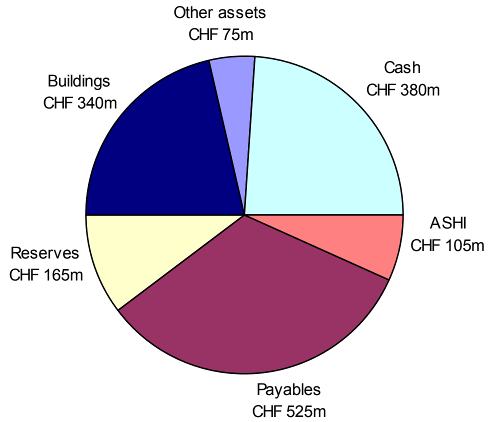
I. COMPARATIVE TABLE: OPTIONS UNDER CONSIDERATION FOR THE FINANCING OF THE WIPO ASHI LIABILITY

OPTION		PROS	CONS
1	The budget would be charged 2% of payroll costs (corresponding to approximately 3.5 million Swiss francs per year). Of this amount, approximately, 1.5 million Swiss francs would be utilized to cover the cost of payments for accumulated leave and repatriation grants as staff members separate from service and WIPO's share of retiree health insurance payments. Any remaining balance would be used to offset the increase in ASHI liability.	Minimal charge to the budget	• the reserves will be reduced by 8.0-9.0 million Swiss francs per year due to the growth of the ASHI liability; • the liability increases; • the problem remains and gets worse
2(a)	The budget would be charged by 9% of payroll costs (corresponding to approximately 16.2 million Swiss francs per year).	The charge is acceptable to the budget.	• the growth in the ASHI liability would continue at the same rhythm for the first five years; • the drain on the reserves would continue at the same rhythm for the first five years but would be subsequently reduced.
2(b)	The budget would be charged by 6% of payroll costs (corresponding to approximately 10.8 million Swiss francs per year).	• the ASHI liability would be funded within about 30 years; • the amount of reserves would be stabilized.	• the use of a substantial level of budgetary resources would be required and this would seriously affect the Organization's programs; • funding over a 30-year period is too long, changes in parameters such as sickness premiums, mortality rate and discount rates may hamper the final result.
3	• The budget would be charged 6.5% of payroll costs corresponding to approximately 11.7 million Swiss francs per year, including funds to cover the payments for separation benefits such as accumulated leave and repatriation grants (currently costing about 0.9% of payroll costs) and WIPO's share of retiree health insurance premiums;	• acceptable charge to the budget; • ASHI amounts secured; • the ASHI liability would be funded within about 19 years.	• during the 19 year period, reserves would initially continue to be reduced. This would be stabilized when sufficient funds had been accumulated for annual investment earnings to help offset the annual growth of the liability; • funding over a 19-year period is long.

OPTION		PROS	CONS
	• a separate ASHI fund would be created, with funds invested in long-term Swiss franc bonds.		
4(b)	• The budget would be charged 6.5% of payroll costs (corresponding to approximately 11.7 million Swiss francs per year) which would include funds to cover payments for separation benefits such as accumulated leave and repatriation grants and WIPO's share of retiree health insurance premiums. • A cash transfer of 50 million Swiss francs would be made from WIPO's balance sheet to a separate entity's balance sheet.	• acceptable charge to the budget; • the ASHI liability would be fully funded over approximately 12 years; • for the first 8 years the reserves would decline only slightly until the accumulated funding in the separate entity begins to earn sufficient revenue to cover the increase in the ASHI liability incurred each year; • over the long-term, WIPO's reserves would be preserved and may actually improve toward the end of the 12 year period when full funding is achieved, depending upon the rate of return generated by the invested fund held by the separate entity.	• funds would remain in the separate entity and would only be returned to WIPO if the total amount held by the entity were to exceed the total ASHI liability.

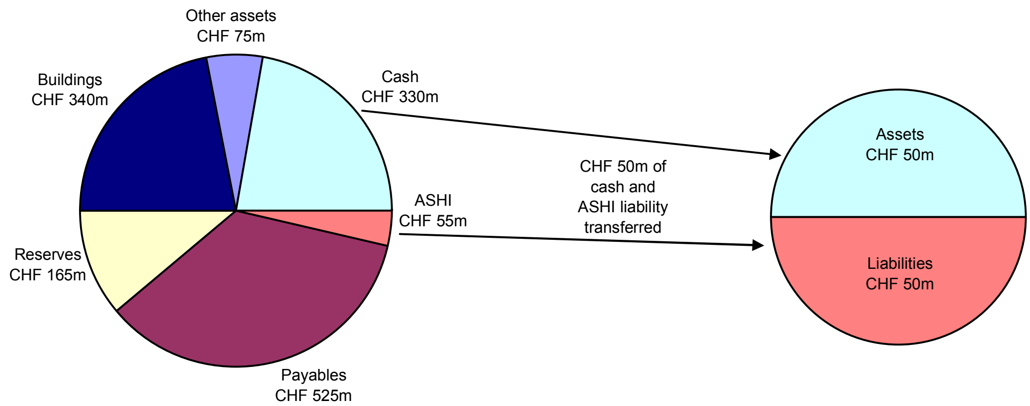
II. FUNDING OF ASHI LIABILITY BY THE PROGRESSIVE FUNDING OF A SEPARATE ENTITY (OPTION 4)

WIPO balance sheet (current)

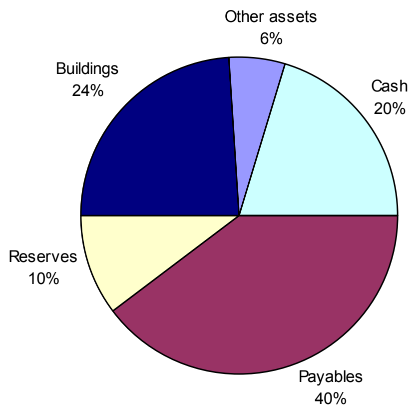


WIPO balance sheet (year 1)

WIPO ASHI entity balance sheet



WIPO balance sheet (year 12)



Although absolute amounts cannot be accurately projected (and therefore percentage balances are shown), after 12 years the ASHI liability has been entirely transferred from WIPO to the WIPO ASHI legal entity as full funding is achieved.

[End of Annex and of document]